

A black and white photograph of the Michigan State Capitol dome, partially obscured by the silhouettes of trees in the foreground. The dome is a large, rounded structure with a pointed top, and the trees are dark and leafy, framing the building.

Michigan Tax Text 2012

Department of Treasury

2012 TAX TEXT

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OVERVIEW

MICHIGAN DEPARTMENT OF TREASURY 2012 TAX TEXT

The Michigan Tax Text is prepared by Michigan Department of Treasury (Treasury) to assist tax preparers in understanding Michigan taxes and in preparing tax returns. There have been significant changes in business taxes and individual income taxes for the 2012 tax year and this text strives to provide the latest and most accurate information available. Treasury continues to develop policy responses as issues arise and the best way to stay informed of the most recent guidance is to visit Treasury's Web site at www.michigan.gov/taxes.

The Individual Income Tax Act was amended, eliminating the special exemption for seniors, some subtractions, and many of the nonrefundable credits. The Homestead Property Tax Credit and Home Heating Credit remain, but eligibility criteria has been significantly changed. Many claimants may receive smaller credits or will no longer be eligible for the credits. In addition, pension and retirement income may be taxable, depending on the age of the retiree. (Refer to Individual Income Tax chapter for specific details on these changes.)

The Michigan Business Tax (MBT) has been replaced by the Corporate Income Tax (CIT), although some filers holding certificated credits may elect to continue to file the MBT until those credits are exhausted. (Refer to the MBT and CIT chapters for further information.)

Accompanying the creation of the CIT is a new withholding requirement for flow-through entities that have members, partners, or shareholders that are corporations or other flow-through entities. A new chapter, Flow-Through Withholding (FTW), is included in this year's publication to provide guidance on changes to the existing flow-through entity withholding on nonresident individual members and on the new withholding requirement on corporations and other flow-through entity members.

The Health Insurance Claims Assessment (HICA) is an assessment that replaces the use tax levied on health care providers. This assessment is a one percent fee due on the "paid claims" made by carriers, third party administrators, and self-insured entities. Also, new this year is information regarding the State Real Estate Transfer Tax (SRETT), as Treasury is experiencing an increase in the number of refund claims received. (Refer to the Special Taxes and Assessments chapter for further information.)

For additional clarification, refer to the Contact List in the Administrative Information chapter, or visit Treasury's Web site at www.michigan.gov/treasury. There are Frequently Asked Questions (FAQs) and other guidance available on the Web site to assist in understanding the tax changes and in preparing accurate tax returns.

ADMINISTRATIVE INFORMATION

2012 UPDATE

Self-Service

Treasury Self-Service options represent the most easily accessible (24 hours a day, 7 days a week) and fastest way for taxpayers and authorized representatives to check on the status of tax returns, get a summary of estimated payments, or ask a question about tax accounts. Taxpayers and authorized representatives are encouraged to use these channels to get information quickly and efficiently. For direct access to Individual Income Tax (IIT) account information, call (517) 636-4486 or access Treasury's Web site at www.michigan.gov/iit. For direct access to business tax account information, access Treasury's Web site at www.michigan.gov/bustax or call (517) 636-6925 for Sales, Use, and Withholding (SUW) taxes (including payroll withholding, pension withholding, and flow-through withholding), MBT/Single Business Tax (SBT), CIT or Business Tax Registration.

Treasury has stringent security measures in place for customers to access account information. Customers are asked to authenticate by entering a combination of shared secrets for security reasons (e.g., Adjusted Gross Income (AGI), Total Household Resources (THR), Household Income (HHI), Gross Receipts, Account/Social Security number (SSN), etc.) before information can be accessed.

From either the IIT or business taxes page, taxpayers may choose the service they wish to access. Additional shared secrets may be required depending on the request. Tax preparers should use the Practitioner Web Services at www.michigan.gov/taxes located under the "Tax Practitioner" button.

Individual Income Tax Self-Service

Visit Treasury's Web site at www.michigan.gov/iit to check items listed below, or call (517) 636-4486.

- Date Treasury is currently processing returns
- If and when a refund, credit claim, or energy draft has been issued for the current year and three prior years
- If a refund, credit, or energy draft has been returned to Treasury, direct deposited into an account, or offset to a debt
- Estimated tax payments
- The status of a letter sent to Treasury
- Ask a question related to the account or check the status of a service request
- Ask a tax preparation question.

Business Taxes Self-Service

Visit Treasury's Web site at www.michigan.gov/bustax to verify items listed below or call the automated phone system at: (517) 636-6925 for SUW, MBT/SBT or Business Tax Registration.

- Tax payments
- Change of address
- Information about payments made by Electronic Funds Transfer
- Request for additional copies of SUW returns
- Request for additional copies of Sales Tax License
- Sales Tax License number
- Status of a letter sent to Treasury
- Status of returns
- Ask a question related to the account or check the status of a previous request
- Ask a tax preparation question.

Tax preparers with account specific questions on individual or business accounts should use the Practitioner Web Service at www.michigan.gov/taxes. The services are for tax preparers only. This information should not be given to others. Call (517) 373-0616 to obtain a user name and password. When using the Practitioner Hotline or Practitioner Web Services, leave a detailed message. If inquiry is account specific, an acceptable online disclosure authorization is required by Treasury before account information will be shared. An *Authorized Representative Declaration (Power of Attorney)* (Form 151) or written authorization may be faxed to (517) 636-5340. (Refer to the Disclosure Guidelines section in the Administrative Information chapter.)

Income Tax Terms Used in Treasury Income Tax Self-Service

Current Tax Year: The current tax year is 2012.

Date Processed: Date Treasury posted return to its computer system. This does not indicate completion of the return.

Completed: Treasury has completed processing the return. The transaction screen will indicate what the taxpayer can expect from Treasury. This includes refund information and whether a refund was direct deposited, applied as a credit to the following year, or offset and applied to a debt.

Issued: A check or Direct Deposit has been issued. 10 to 14 business days should be allowed for mail to be received. Direct Deposits can take up to five days from the completed date to post to the taxpayer's account. Verify the refund amount is the amount Treasury has indicated. If the refund amount is not in the account after five days, the taxpayer should contact their financial institution. If there is a problem with the Direct Deposit, Treasury will normally issue a refund check.

Manual or Pending Review: By law (Michigan Compiled Law (MCL) 205.28(1)(f)), Treasury cannot disclose to anyone why a return has been selected for manual review. Treasury has established procedures for selecting returns for manual review both to protect citizens and to ensure appropriate amounts are being refunded. If a taxpayer's return has been selected for review, additional time for processing is required.

Pending Response: Treasury is unable to complete the return without additional information from the taxpayer. It could take an additional 12 weeks from the date a response is received by Treasury for the return to be completed. If more than 12 weeks have passed, contact the Practitioner Web Services.

State Debt or Third-Party Debt: If Self-Service indicates a refund was used to pay a “State debt or third-party debt,” it could take three to four months (depending on the type of debt) for the refund amount to be applied to the debt. The message on Self-Service will provide taxpayers with a phone number to call and they will also receive a letter.

Emergency Refunds or Hardship Cases: Taxpayers requesting an expedited refund due to a hardship situation must provide documentation of foreclosure, eviction, or utility shutoff with their requests.

Why Self-Service Might Indicate Treasury Has Not Received an Income Tax Return

Self-Service may indicate an income tax return hasn’t been received due to the following reasons:

- SSN provided may not match Treasury records.
- Taxpayer filed an amended return. Amended returns are reviewed late in the year; they should be entered into Treasury’s computer system within eight weeks of receipt.
- Taxpayer’s information is in the process of being posted. The system is updated once every business day. It is possible to call on Monday and find no record of a taxpayer’s return and then call on Tuesday and learn the return posted overnight.
- It can take eight weeks for paper return information to be entered into Treasury’s computer system. If the Web site or Customer Contact number does not state a return has been received ten weeks after the return was mailed, contact Practitioner Web Services through e-Service.

Note: Timelines above are approximate.

E-Registration for Michigan Taxes

Michigan Business One Stop (MiBOS) is a fast, easy, and secure way to register a business for taxes in the State of Michigan (State). This site allows taxpayers to perform a variety of tasks involved in starting and operating a business, including applying for permits and licenses. Businesses must have a Federal Employer Identification Number (FEIN) to register and may register for most Michigan business taxes, as well as an Unemployment Insurance Agency (UIA) account number, or a Sales Tax License using the online e-Registration application at www.michigan.gov/business.

This process is easy, secure, convenient, and faster than registering by mail. It eliminates the need to mail *Registration For Business Taxes* (Form 518). After completing the online application, taxpayers will receive a confirmation number for their electronic submission.

Businesses can receive their:

- Sales/Use Tax license within seven to ten days.
- New UIA employer account number within three business days.

MiBOS also provides additional information in the FAQs and “Resource Center” sections, which can be accessed by selecting these links. There is also online help throughout the process in the form of content-specific help links and pop-up messages.

Use e-Registration when starting a new business that will engage in any of the following activities:

- Sell or lease tangible personal property in Michigan to the final consumer
- Will owe SUW, Motor Fuel, MBT, or Tobacco taxes
- Will have employees performing services in Michigan
- Plans to have employees working in Michigan
- Submit notice of change of entity type for an existing business (e.g., from sole proprietorship or partnership, incorporate a sole proprietorship or partnership) or acquire all or any part of the assets, organization, trade, or business of an existing business having employees in Michigan. **(A taxpayer cannot continue to use the FEIN of a prior owner; the taxpayer must register for their own FEIN.)**

Do not use MiBOS to register if the business has previously mailed a paper copy of Form 518 to Treasury.

Begin the process by setting up a User Account. Business representatives can create their own User Accounts enabling them to complete and store multiple applications. Completed tax registration applications will be stored for viewing for 30 days; incomplete applications will be stored for six months.

DISCLOSURE GUIDELINES

Treasury employees are bound by disclosure laws as stated in Michigan Compiled Law [MCL 205.28(1)(f)] and the federal penal code. Employees of the Michigan Accounts Receivable Collection System (MARCS), an agency under contract with Treasury, are bound by the same disclosure requirements as Treasury employees. The law prohibits the disclosure of confidential tax information to any person other than the taxpayer of record, unless the taxpayer authorizes the disclosure of his or her information to another individual.

Acceptable disclosure authorizations are:

- *Authorized Representative Declaration (Power of Attorney)* (Form 151)
- Copy of Internal Revenue Service (IRS) form 2848 Power of Attorney and Declaration of Representative if modified to reference Michigan tax return information.
- Checking the Authorization box on the Michigan income tax return(s) (only information on the return will be discussed with the tax preparer).
- Written consent with taxpayer’s signature.
- Verbal/implied consent (e.g., conference call, interpreter, translator).

Form 151 is available on Treasury's Web site at www.michigan.gov/taxes, by calling (517) 636-4486, or by writing to:

*Michigan Department of Treasury
Customer Contact Division
P.O. Box 30757
Lansing, MI 48909*

Direct questions on disclosure guidelines by calling (517) 636-4239, faxing (517) 636-5340, or writing by way of overnight courier to:

*Michigan Department of Treasury
Office of Privacy and Security
Disclosure Unit
7285 Parsons Dr.
Dimondale, MI 48821*

For USPS mail delivery, send to:

*Michigan Department of Treasury
Office of Privacy and Security
Disclosure Unit
P.O. Box 30791
Lansing, MI 48909*

IDENTITY THEFT

Both the IRS and Treasury have seen an increase in the number of fraudulent returns being filed by individuals using stolen identities or "false" SSN. Unfortunately, legitimate filers' returns are often received after the fraudulent return, slowing down the issuance of accurate refunds due the "real" filer. Indicators of fraud are:

1. Upon filing, the legitimate taxpayer receives a message that the return has already been filed, either by letter (if a paper return is filed) or by the transmitter of an electronically filed return.
2. An original return filed by the "legitimate" taxpayer is processed as an amended return, even though the original (fraudulent return) return reports different figures.
3. The refund return is processed as a tax due return, because of a previous refund issued on the fraudulent return.

If a taxpayer or a preparer's client receives any indication that the original return is rejected as a duplicate or an amended or tax due return, please submit any information requested by Treasury. Treasury will request items of documentation such as W-2 statements, drivers' licenses or state-issued identification cards and any information provided to the filer by the IRS to verify the valid return. Do **not** send originals when submitting documents to Treasury for review.

Refer to Treasury's Web site for additional information at www.michigan.gov/taxes.

TAXPAYER RIGHTS AND RESPONSIBILITIES

Treasury employees comply with Michigan law by providing:

- Prompt, fair, and courteous service
- Confidentiality
- Timely processing of returns
- Copies of tax returns and related documents from a taxpayer's file.

If Treasury fails to provide these services, taxpayers have the right to file a complaint. Taxpayers should note the name of the person they dealt with so the complaint can be handled properly. It is the taxpayer's responsibility to:

- File returns on time with the correct payment (if necessary)
- Make sure returns are correct, no matter who prepares them.

The Billing Process

If Treasury believes additional tax is owed, the following actions will be taken:

1. Sending a letter stating the amount due and why it is due. If the taxpayer agrees with the amount due, it should be paid immediately. If the taxpayer has questions or is in disagreement with the amount due, they should contact Treasury right away using the address or telephone number in the letter.
2. Thirty days after the letter, a *Notice of Intent to Assess* for the taxes due is issued. If the taxpayer disagrees with the amount due, they may request an informal conference within 60 days of this notice (see "*The Appeals Process*" section).
3. Sixty days after the Notice of Intent to Assess, a Bill for Taxes Due (Final Assessment) is issued unless Treasury has received correcting information (see "*The Appeals Process*" section).

Payment of the Additional Tax

1. Payments may be made at any time during the billing process. If all the taxes due cannot be paid, contact the Collection Division at the telephone number on the notice to request an installment agreement.

2. Payment **must** be made within 35 days of the final assessment. If full payment is not made, the following actions may be taken by Treasury (whether or not there is an installment agreement):
 - Intercept paychecks or levy bank accounts.
 - Place liens on home, business, or personal property to protect the State's interest as a creditor.
 - Refer the account to Treasury Field staff or MARCS to actively pursue collection of the debt.
 - Intercept any money the State owes a taxpayer (such as an income tax refund) and apply it to the debt.
 - Apply penalty and interest for as long as there is a tax balance. (All payments are applied first to interest, then to penalty, then to tax).

Jeopardy Assessments for Extreme Cases

If, at any time, Treasury believes a taxpayer plans to sell and/or hide property to avoid seizure, a jeopardy assessment and lien(s) will be issued to freeze assets. This means the taxpayer will not be able to withdraw money from bank accounts or transfer the title of any property. If a taxpayer wishes to sell property, Treasury will send a representative to the sale to accept payment of the liability. The actions of levy and jeopardy assessment are severe. Give prompt attention to resolving a debt when contacted.

The Appeals Process

Taxpayers have the right to appeal any billing or final decision of Treasury's.

Informal Conference (Hearing):

1. For an informal conference with a Treasury referee, write to Treasury within 60 days after receiving a Notice of Intent to Assess or notice of a final decision. Include the following in the written request:
 - Name
 - Taxpayer identification number
 - The amount of tax disputed
 - An explanation of the dispute
 - Payment of any portion of the tax bill not disputed.
2. A hearing date and time is set that is convenient for all parties.
 - Treasury may require that a hearing be held by telecommunications for efficient tax administration, or a taxpayer may request to participate in the hearing by telecommunications.

- Taxpayers may be assisted by an attorney or other representative or have someone represent them in their absence by filing a completed Form 151 authorization.
 - Taxpayer may record the hearing, but must notify Treasury at least seven days ahead of time.
3. The referee will make a recommendation to the State Treasurer's designee who will review the file, make a final decision, and notify the taxpayer.

Tax Tribunal or Court of Claims:

4. Taxpayers may appeal the State Treasurer's decision from an informal conference or a final assessment to either:
 - The Michigan Tax Tribunal within 35 days, which requires payment of the undisputed amount.

Or

 - The Court of Claims (Ingham Circuit Court) within 90 days, which requires payment of the full amount of the assessment.
5. Decisions of the Tax Tribunal or the Court of Claims may be appealed to the Court of Appeals and ultimately to the Michigan Supreme Court.

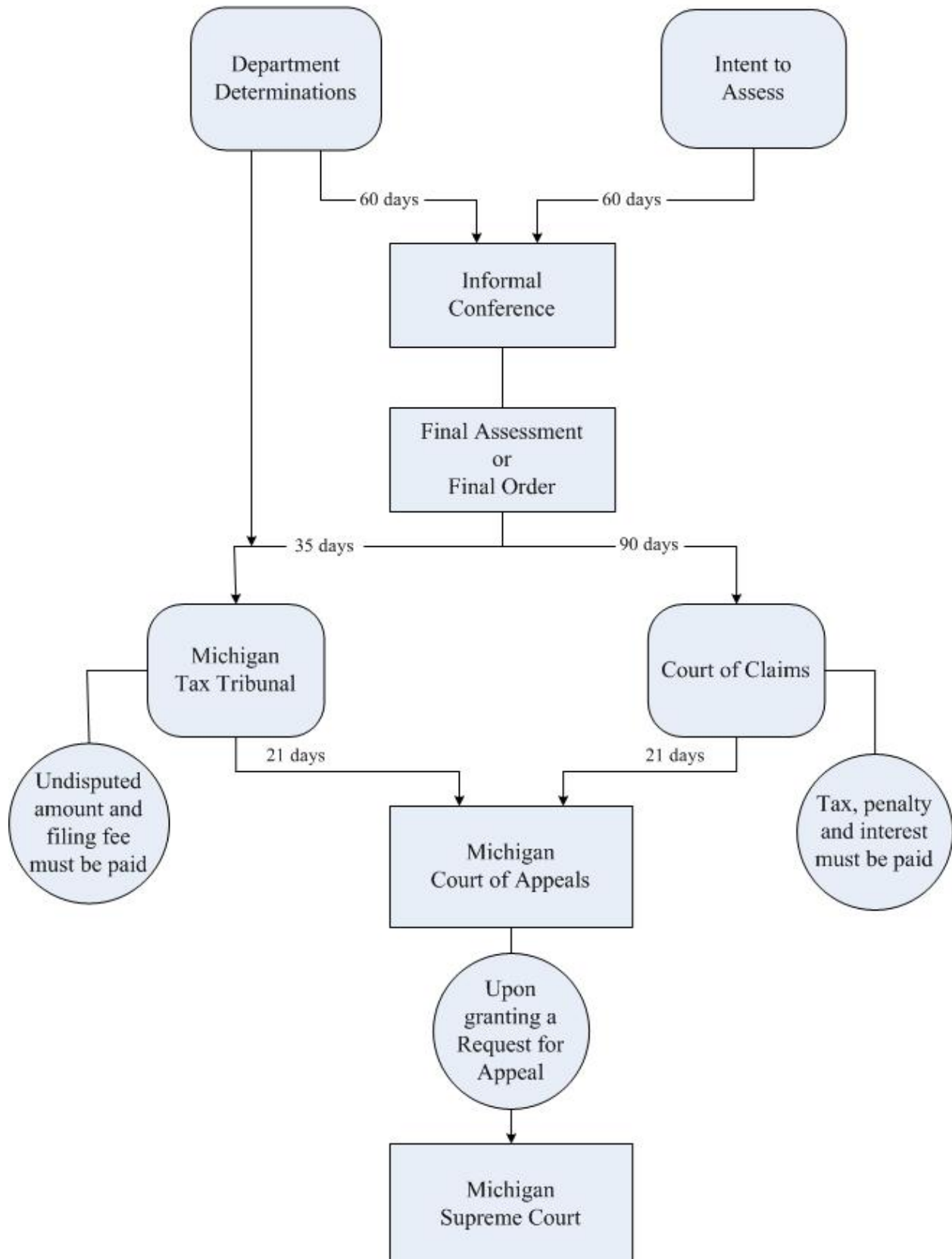
Claiming a Refund

Many people have Michigan income taxes withheld from their wages. If taxes are not withheld or the amount owed on an annual return is more than \$500, a taxpayer must estimate income tax and pay it quarterly. If not, a bill may be issued for additional penalty and interest. If a taxpayer believes they have overpaid taxes and may be due a refund, a tax return (MI-1040) must be filed to claim the refund. Taxpayers have four years from the date the return is due to claim a refund. Income tax refund claims filed on or before April 18 for the preceding tax year that are accurate and complete are usually processed by June 1. Interest is added to the refund beginning 45 days after the claim is filed, or 45 days after the due date established by law for filing the return, whichever is later.

Refund Different Than Expected

Treasury will send a statement explaining the reason the refund amount is different than expected. For adjustments to IIT and CIT/MBT returns, letters will include line changes to assist taxpayers in understanding adjustments. If a taxpayer disagrees with the adjustment, they may request an informal conference by writing to Treasury within 60 days of the date on the refund statement. Mail correspondence to the address provided on the refund statement. (Refer to Appeal Procedure flow chart on next page for an overview of the appeal process).

**MICHIGAN DEPARTMENT OF TREASURY
REVENUE ACT
APPEAL PROCEDURE**



ADMINISTRATIVE DISPUTE RESOLUTION

Treasury makes every effort to resolve taxpayer account problems/disputes at the lowest possible level. If a taxpayer has been unsuccessful in resolving a problem through normal channels, they should contact the Taxpayer Advocate. The Taxpayer Advocate is charged with prompt resolution of disputes, including return problems, billing issues, and collection disputes. The Taxpayer Advocate represents the interests of individual taxpayers, business taxpayers, and the taxpaying public in the policy and operations areas. The Problem Resolution Office (PRO) is an adjunct to the Advocate's office.

Tax preparers receive priority service from the PRO. They can contact the PRO by telephone through the Practitioner Hotline and leave a voice mail, or online through Practitioner Web Services. This ensures immediate acknowledgment of the tax preparer's inquiry. Tax preparers **must not** give the telephone number, user ID, and password to their clients.

Contact information for these areas include:

*Michigan Department of Treasury
Taxpayer Advocate
P.O. Box 30698
Lansing, MI 48909-8918*

Fax: (517) 636-4254

Practitioner Hotline (Not for Public Use)

(517) 373-0616

Practitioner Web Services (Not for Public Use)

www.michigan.gov/taxes

FORMS

Availability of Tax Year 2012 Forms

Current year forms are available by calling (517) 636-4486 after February 1, 2013.

Current and prior year forms are available on Treasury's Web site at www.michigan.gov/taxes.

Address mail orders to:

*Michigan Department of Treasury
Customer Contact/Forms Request Unit
P.O. Box 30757
Lansing, MI 48909*

Use personalized forms whenever possible. Personalized forms ensure the correct account is credited. **Never photocopy** personalized forms for someone else's use. Personalized forms are coded with the taxpayer's SSN(s) or account numbers (FEIN, Michigan Establishment (ME), or Treasury-assigned (TR) numbers) and are specifically assigned to businesses and optically scanned. Coded information is machine readable on photocopies and through correction tape and fluid. As a result, an incorrect account may be credited.

Filing Due Dates

Filing due dates for the various individual, business, and miscellaneous taxes are as follows:

<u>Tax</u>	<u>Due Date</u>
Individual Income Tax	April 15
Individual Tax Estimates	April 15, June 15, and September 15 of tax year and January 16 of following year
Fiduciary Tax	On or before 15 th day of fourth month after close of tax year
Fiduciary Tax Estimates	April 15, June 15, and September 15 of tax year and January 16 of following year
Home Heating Credit Claim	September 30 immediately following tax year for which credit is claimed
Sales Tax	Monthly Filer - on or before the 20 th of the following month with a discount for early or timely remittance Quarterly Filer - on or before the 20 th of the following month with a discount for early or timely remittance Annual Filer - February 28 with discount for timely remittance
Use Tax	Same as Sales Tax
Payroll or Pension Withholding Tax	Monthly Filer - on or before 20 th day of following month Quarterly Filer - on or before the 20 th day of month following quarter Annual Filer - February 28
Flow-Through Withholding Tax	Quarterly returns on or before the 15 th day of the month following the end of the quarter Annual return on or before the last day of the second month after the end of the tax year

<u>Tax</u>	<u>Due Date</u>
Corporate Income Tax (replaced Michigan Business Tax effective January 1, 2012)	Calendar Year Filer - April 30 Fiscal Year Filer - last day of 4 th month after end of tax year. For tax years ending in 2011, all returns are due April 30, 2012 unless an extension is obtained.
Michigan Tobacco Tax Return (322)	20 th of each month following reporting period
Tobacco Products Licenses (336)	Annually by July 1

International Fuel Tax Agreement (IFTA)

- Renewal Application for Michigan IFTA Fuel Tax License (3014) Annually by January 1
- IFTA Return (IFTA-100-MN and IFTA-101-MN) Last day of month following the end of quarter

Motor Fuel

- Fuel Importer Return (3992) 20th of month following end of quarter
- Exporter Quarterly Report (4004) 20th of month following end of quarter
- Liquefied Petroleum Gas Tax Return (577) 20th of month following end of quarter
- Marine Retail Diesel Tax Return (3769) 20th of month following end of quarter
- Fuel Supplier Return (3978) 20th of every month
- Terminal Operator Annual Return (3877) On or before February 25 of following year
- Terminal Operator Monthly Report (3716) 20th of every month
- Three-Day Payment Voucher (3778) Three business days after taxable event
- Transporter Quarterly Report (3724) 20th of month following end of quarter
- Blender (3791) 20th of every month
- Bonded Importer Estimated Payments (3819) 20th of every month
- Carrier Report (3715) 20th of every month

Severance Tax

- Severance Tax (382) 25th of month following the report month

PENALTY AND INTEREST

The Revenue Act's provisions for penalty and interest are as follows:

**Civil Penalties Imposed
Under the Revenue Act
(Public Act 122 of 1941, as Amended)**

Section No.	<u>Condition</u>	<u>Provision</u>
19(3)	Non-negotiable remittance	\$50
21(3)	Frivolous protest	\$25 or 25% of the tax due, whichever is greater
23(2)	Interest	1% above the prime interest rate to be adjusted on January 1 and July 1 of each year
23(3)	Negligence	10% of the deficiency (minimum \$10)
23(4)	Intentional disregard of the law	25% of the deficiency (minimum \$25)
23(5)	Civil fraud	100% of the deficiency
24(2)	• Failure or refusal to file a return	5% of the tax due for the first two months, then 5% per month of the tax due (maximum 25%)
24(2)	• Failure or refusal to pay a tax	5% of the tax due for the first two months, then 5% per month of the tax due (maximum 25%)
24(5)	• Failure or refusal to file an informational return	\$10 per day (maximum \$400)
30	Interest on refund returns	1% above the prime interest rate to be adjusted on January 1 and July 1 of each year

**Criminal Penalties Imposed
Under the Revenue Act
(Public Act 122 of 1941, as Amended)**

<u>Section No.</u>	<u>Condition</u>	<u>Provision</u>
27(2)	False or fraudulent return or false statement in return	Felony (maximum fine of \$5,000, imprisonment for not more than five years, or both)
27(1)(b)(c)	Aid, abet, or assist another in attempt to evade the payment of a tax, or part of a tax, or file false claim for credit or refund, either in whole or in part	Felony (maximum fine of \$5,000, imprisonment for not more than five years, or both)
27(3)	Perjury (a person knowingly swears to or verifies a false or fraudulent return or a return containing a false or fraudulent statement, with the intent to aid, abet, or assist in defrauding the State)	Fines and/or imprisonment as provided under the general provisions of the Michigan Compiled Laws. This may be imposed in addition to the provisions of Section 27(1) and (2) of the Revenue Act.
27(4)	Person is not guilty under subsection (2) but knowingly violates any other provision of this Act	Misdemeanor (fine of not more than \$1,000, or imprisonment for not more than one year, or both)

Interest

The interest rate for tax due and refunds is the prime rate plus one percent, adjusted on January 1 and July 1. Interest on refunds is computed from 45 days after the return is filed or 45 days after the due date of the return, whichever is later. (Refer to the most current Revenue Administrative Bulletin (RAB) in the Reference Library on Treasury's Web site at www.michigan.gov/treasury or www.michigan.gov/taxes).

Waiver of Penalty

The Revenue Act governs the penalty on tax due. The taxpayer has the option to request waiver of penalty, and Treasury will grant a waiver if the taxpayer demonstrates reasonable cause existed which prevented timely payment of the tax due. Examples of reasonable cause are: death or serious illness of the taxpayer or the individual primarily responsible for filing returns and making tax payments; extenuating circumstances (e.g., fire, theft, or criminal acts against the taxpayer; or misapplication of payments by Treasury). Lack of funds or poor bookkeeping practices do not constitute reasonable cause for waiving penalty.

All requests for waiver of penalty must be made in writing and must explain why the waiver is being requested. Requests for waiver of penalty should be directed to the Customer Contact Division for consideration.

INTERCEPTING REFUNDS

The Revenue Act **requires** Treasury to intercept any monies due to a taxpayer and to apply those funds to outstanding State debts. Treasury will intercept and apply tax refunds, overpayments from assessments, and vendor payments. Tax debts or money owed to other agencies such as Department of Human Services, Department of Community Health, or Friend of the Court are collected by Treasury, as are defaulted student loans. Treasury also receives court orders for garnishment of tax refunds, which requires Treasury to intercept tax refunds and send those monies to the garnishing agency. If the taxpayer files jointly and their spouse is not liable for the debt, the taxpayer will receive a form which allows the non-obligated spouse to compute and claim their portion of the tax refund.

WEB SITE

Treasury's Web sites www.michigan.gov/treasury and www.michigan.gov/taxes offer information about property taxes, unclaimed/abandoned property, revenue, local governments, and investments. RABs, tax forms, statute, court cases, FAQs on a number of issues, and contact names and numbers may also be found by visiting the Web sites.

CONTACT NUMBERS

For answers to specific tax questions, call the appropriate number listed below:

Income Tax	(517) 636-4486
Michigan Business Tax	(517) 636-6925
Motor Fuel Tax	(517) 636-4600
Motor Carrier Tax	(517) 636-4580
Sales, Use, and Withholding Taxes	(517) 636-6925
Single Business Tax	(517) 636-6925
Tobacco and Cigarette Taxes	(517) 636-4630

Assistance is available using TTY through the Michigan Relay Service by calling 1-800-649-3777 or 711. Printed material in an alternate format may be obtained by calling (517) 636-4486.

For assessments, payments, and/or payment arrangements, contact Collection Division at (517) 636-5265.

Contact List on Web

The Treasury Contact List is available on Treasury's Web sites at www.michigan.gov/treasury and www.michigan.gov/taxes. This list is updated as changes occur.

Protect Your Privacy

Because the Internet is not a secure environment, **never** send confidential information (e.g., SSNs, tax account numbers) over the Internet. To further protect taxpayers' privacy, Treasury will not send sensitive or confidential information over the Internet in response to e-mail inquiries. To receive a response to an account-specific issue, use the "Ask Treasury a Question" option in the Self-Service section of the Web site (www.michigan.gov/iit or www.michigan.gov/bustax).

To ensure the privacy of account information, mail inquiries (via U.S. mail) to the appropriate tax or administrative division at Michigan Department of Treasury, Lansing, Michigan 48922. Include complete name, address, and SSN (or FEIN for businesses).

Treasury is not responsible for the misdirection or misuse of any information which may be transmitted via e-mail across the Internet.

HELPFUL INFORMATION

Calling

Always have the letter, notice of inquiry, notice of adjustment, assessment, etc., available for reference. Always read the entire letter before calling and then call the number provided. If referring to a notice of adjustment that has been faxed, make sure the back of the notice is included. The back of the notice of adjustment includes an explanation of all adjustments to the return and/or payments.

A phone call does not constitute a response to Treasury letters. A valid response is mailing the documentation requested in the correspondence, along with any necessary explanations.

If staff is not available to take the call, leave a detailed voice mail message (only available on the Practitioner Hotline). Include the following information:

- Taxpayer's name and phone number
- Taxpayer's TR number, FEIN, or SSN
- Years for which taxpayer is being contacted
- Any other pertinent information.

Writing

Always mail a copy of Treasury's correspondence with the response. This will help route correspondence to the proper person in a timely manner.

- Include TR number, FEIN, or SSN on all correspondence.
- Include daytime telephone number.
- Address correspondence to the name or unit listed on the correspondence.
- If mailing returns, always keep a copy. Treasury does not mail back original returns.
- Be sure to submit documentation for all the years in question, not just the years for which there is a liability.

Making a Payment

- **Always** write TR number, FEIN, or SSN on the check.
- **Always** indicate the type of tax and the tax year/period being paid (e.g., MBT, CIT, IIT, SUW, etc.). In the event the check gets separated from the return or documentation, the payment can be properly applied to the account.
- If submitting multiple returns for one particular tax, one check can be written for the total amount due.
- If paying more than one type of tax, it is best to write a separate check for each tax and mail the checks to the address indicated on the return.
- Never send a check or money order without some form of documentation. This could cause a lengthy delay in determining what the payment is for.

Treasury Letters

Treasury sends letters to taxpayers for a variety of reasons. It is very important for taxpayers to read their letters carefully and respond as directed in the letter. Some of the more frequent types of letters are:

- If Treasury is unable to process a return with the information provided, a letter of inquiry may be sent requesting additional information. If a taxpayer receives a letter of inquiry, respond in writing within 30 days, sending a copy of the original letter and all the requested information to the address provided in the letter. Failure to respond or provide all of the information requested may result in the denial or reduction of refunds, or in additional tax due.

- If the review of a return results in adjustments, Treasury will send the taxpayer a letter of explanation. If the taxpayer disagrees with the adjustments, he or she must write to Treasury requesting a re-evaluation. The letter must state why the taxpayer believes the adjustments are incorrect and should include documents to support the claim.

Taxpayers should always keep a copy of any correspondence sent to or received from Treasury. For questions regarding a letter, call the number provided on the letter or the number for the specific tax involved to speak with a customer service representative.

E-mail LISTSERV for Tax Professionals

The Treasury Tax Professionals' LISTSERV is a free service that disseminates mass e-mail messages to all subscribers. This includes electronic communications on Treasury's e-file programs and other information of interest. To subscribe to this service or for additional information, visit www.Mifastfile.org and select Tax Preparer.

SUMMARY OF UNCLAIMED PROPERTY LAW

Under Michigan's Uniform Unclaimed Property Act (Public Act 29 of 1995, MCL 567.221, et. seq.), holders of unclaimed property are required to report and remit unclaimed property belonging to owners whose last known address is in Michigan. Unknown owner or unknown address property must be escheated to the holder's state of incorporation. Most businesses, including financial institutions, have unclaimed property resulting from normal operations, such as, uncashed checks (e.g., payroll, vendor, dividends, etc.), account receivable credit balances, unredeemed gift certificates, dormant bank accounts, uncashed money orders and travelers checks, unclaimed security deposits, shares of stock and associated dividends, and contents from safe deposit boxes. Businesses must file an annual holder report and remit the property to Treasury, Unclaimed Property Division.

Who Must Report

Every business or government agency holding unclaimed property belonging to someone whose last known address is in Michigan must report. If the holder is incorporated in Michigan and the owner's last known address is unknown or is in another state or country and the holder does not report under the provisions of that state or country, then the holder must report those interests to Michigan.

What Must Be Reported

Generally, tangible and intangible property belonging to another party that has gone unclaimed for a specified period of time is considered unclaimed property and must be reported. The dormancy period for most property types is three years with some exceptions. For example, uncashed payroll checks must be turned over after one year of dormancy. Government agencies must also turn over unclaimed property after one year of dormancy. Visit Treasury's Web site at www.michigan.gov/unclaimedproperty for more information about property types and dormancy periods.

Reporting Due Date and Penalty for Noncompliance

All items considered unclaimed as of March 31 must be reported and remitted by July 1 each year. Businesses that fail to pay or deliver unclaimed property timely to the State of Michigan may be liable for:

- (1) Interest at the current monthly rate of one percentage point above the adjusted prime rate on the value of the property from the date the property should have been paid or delivered, **and/or**
- (2) Penalty of 25 percent of the value of the property that should have been paid or delivered.

How to Report

The *Manual for Reporting Unclaimed Property* and forms required for reporting can be found on Treasury's Web site at www.michigan.gov/unclaimedproperty. Free holder reporting software is also available on the Web to assist holders in reporting unclaimed property.

Noncompliance With Unclaimed Property Reporting Requirements

Section 31(2) of the Uniform Unclaimed Property Act gives the State Treasurer the authority to conduct unclaimed property examinations (audits) to determine compliance with the Act. Unclaimed property audits conducted by Treasury will cover the last ten reporting years and penalty and interest will be assessed as a result of the audit.

How Owners Locate Unclaimed Property Reported to the State of Michigan

The Unclaimed Property Web site provides an option to search statewide and nationwide for unclaimed property. Persons or entities may also call the Unclaimed Property Division at (517) 636-5320. Twice each year the State of Michigan publishes a notice in a statewide newspaper, which provides information on the number of new unclaimed properties added since the last publication and how persons and entities can search for and claim property that may belong to them. In addition, the Unclaimed Property Division attempts to locate owners of unclaimed property through its outreach efforts.

INDIVIDUAL INCOME TAX

WHAT'S NEW

Legislative Changes to the Michigan Income Tax Act for Tax Year 2012

Public Act (PA) 38 of 2011 and several other public acts contain extensive changes to Michigan's Individual Income Tax (IIT) that will affect individual income tax returns filed for the 2012 Tax Year. The income tax rate was 4.35 percent, but a rate reduction to 4.25 percent occurred on October 1, 2012. The annualized rate for 2012 is 4.33 percent. The personal exemption was \$3,700, but an increase to \$3,950 occurred on October 1, 2012. The annualized personal exemption for 2012 is \$3,763. Many taxpayers will be affected as a result of the changes to the Income Tax Act (ITA). Some of the changes are listed below. Additional information can be found at www.michigan.gov/taxes.

- \$600 deduction for children under age 18 is no longer available.
- \$2,400 special senior exemption is no longer available.
- Special exemption for unemployment compensation is no longer available.
- Some or all pension/retirement benefits may be taxable, depending on taxpayer's filing status and year of birth.
- Homestead property tax credit may be smaller in 2012 or no longer available to many taxpayers in 2012 because of a shift from total household income to total household resources, a lower phase-out level, a cap on the taxable value of a homestead, and because some senior claimants may have the credit reduced from 100 percent to 60 percent.
- Subtractions for political contributions, prizes won from raffles or charity games, certain distributions from IRAs used to pay higher education expenses, gross income from oil and gas without regard to expenses and distributions from a retirement plan that are contributed to a charitable organization are no longer available.

FORMS

Income Tax Forms

Most IIT forms are designed for electronic scanning, which permits faster processing with fewer errors. The IIT Instruction Booklet contains information on how to correctly complete these scannable forms to avoid unnecessary delays caused by manual processing.

Direct Deposit of Michigan income tax refunds is available. Information required for requesting the Direct Deposit of a refund is in the IIT Instruction Booklet.

Direct Deposit is only available when the State is issuing a warrant and only on the first return filed each year. The Home Heating Credit Program sends the credit in the form of an Energy Draft directly to the energy provider or to the claimant. Only a claimant whose heat is included in rent should use *Direct Deposit of Refund* (Form 3174).

Substitute Forms Must Be Approved

Treasury accepts substitute tax forms that meet the requirements of Treasury's Policy ET-03066 Substitute Printed, Computer-Generated, and Electronic Filing Forms/Software. A copy of Policy ET-03066 is available on the Treasury Web site at www.michigan.gov/taxes or by calling Forms and Document Services (FDS) at (517) 335-1179.

Before releasing software to tax preparers, software developers must submit forms for review and receive official approval from FDS. Approvals are granted for one year only.

Substitute forms filed with Treasury that are not approved will be returned to the taxpayer.

Tax forms are available on the Treasury Web site at www.michigan.gov/taxes.

Mailing Addresses

All **paper-filed and Individual returns** should be mailed to the following addresses:

MI-1040:

For refund, credit, or zero returns, mail to:

Michigan Department of Treasury
Lansing, MI 48956

To pay tax due, mail the return and payment to:

Michigan Department of Treasury
Lansing, MI 48929

MI-1040CR-7:

Mail the MI-1040CR-7 to:

Michigan Department of Treasury
Lansing, MI 48956

FEDERAL/STATE AND STATE STANDALONE ELECTRONIC FILING PROGRAM

Nearly 100 million people nationwide know electronic filing (e-filing) is the way to go! Two-thirds (over 3.6 million) of all Michigan taxpayers chose to e-file their tax returns. Thank you for making e-file a success.



Tax preparers who complete 11 or more income tax returns are required to e-file all eligible returns. Software developers producing tax preparation software or computer-generated forms must support e-file for all Michigan income tax forms that are included in the software package.

To optimize operational efficiency and improve customer service, Treasury has joined with the Internal Revenue Service (IRS) by transitioning from the Electronic Management System (EMS) e-file program to the IRS Fed/State Modernized e-File (MeF) program for filing income tax returns. MeF will not change the way tax preparers transmit e-file returns. For tax year 2012, Michigan will accept one return each for 2010, 2011, and 2012 income tax returns through the MeF program when supported by the software.

Ninety-five percent of Michigan taxpayers can e-file their State and federal tax returns. Taxpayers who choose e-file will continue to receive faster refunds. In addition, the software checks the computations before transmission, eliminating data entry mistakes by the filer or data capture process. Treasury also acknowledges receipt of transmitted data within 48 hours from when filed or federal acknowledgment received, overcoming concerns of paper returns being lost in the mail or misplaced. When e-filing federal and State returns together, much of the same data is used so information is entered only once, again lessening the possibility of error.

There are many benefits to tax preparers who participate in the e-file program:

- **Expanded services offered.** E-file is a valuable addition to a tax preparer's list of client services, which can mean more clients. In addition, prospective clients can search for an authorized e-file provider at www.irs.gov.
- **Faster refunds for e-file returns.** E-filed returns are processed faster than paper returns. **Allow 14 days** before checking the status of the e-filed return by visiting www.michigan.gov/iit. Clients can also choose Direct Deposit and have their refunds deposited directly into their accounts at the financial institution of their choice.
- **Improved return accuracy.** Treasury processes the same data the tax preparer enters into the computer. The computer program checks for math errors. If an error occurs on a return, the e-file software sends an error message and allows the tax preparer to immediately correct the mistake before the return is transmitted. There is two-thirds less chance of error compared to a paper return.

- **Detailed error conditions.** MeF business rules pinpoint the location of the error in the return and provide complete information in the acknowledgement file that is passed back to the transmitter. MeF business rules use simple wording to clarify each error that triggers a rejection. Treasury will provide up to ten business rule errors per return submission.
- **Increased customer satisfaction.** Only tax preparers and their client see the return. Tax information is encrypted and transmitted directly to the IRS and Michigan. Also, an acknowledgment is sent to verify the return was received and accepted for processing.
- **Prior year returns.** One tax return each for 2010, 2011, and 2012 will be accepted during the 2013 processing year. As subsequent tax years are added to the system, MeF will accept the current tax year and two prior tax years.
- **PDF attachments.** MeF accepts Portable Document Format (PDF) attachments with e-filed returns. Refer to the *Michigan Tax Preparer Handbook for 1040 Modernized e-File (MeF)* for more information on attachments that will be accepted by Michigan.
- **Authorization to discuss.** Treasury staff can see immediately if the taxpayer has granted authorization to discuss the return with the tax preparer. The delays of ordering paper returns and mailing correspondence are eliminated.

How Fed/State (Linked) Electronic Filing Works

Tax preparers and transmitters accepted into the IRS Fed/State MeF Program may submit federal and/or State returns to the IRS. The State submission can be linked to the IRS submission by including the Submission ID of the federal return. If the State submission is linked to an IRS submission (also referred to as the Fed/State return), the IRS will check to see if there is an accepted IRS submission under that Submission ID. If there is not an accepted federal return for that tax type, the IRS will deny the State submission and a rejection acknowledgment will be sent to the transmitter. Treasury has no knowledge that the State return was denied (rejected) by the IRS. If there is an accepted federal return under that Submission ID, MeF will perform minimal validation on the State submission. The State data will then be made available for retrieval by Treasury. After the State data is retrieved, it will be acknowledged and, if accepted, processed by Treasury.

Note: The IRS recommends if a state submission is linked to an IRS submission, sending the IRS submission first and, after it has been accepted, sending in the state submission.

How State Standalone (Unlinked) Electronic Filing Works

Tax preparers and transmitters accepted in the IRS e-file program may submit State Standalone returns when supported by the software. If the Electronic Return Originator (ERO) does not link the State return to a previously accepted federal return (also referred to as State Standalone return), the IRS will perform minimal validation on the State submission. The State data will then be made available for retrieval by Treasury. After the State data is retrieved, it will be acknowledged and, if accepted, processed by Treasury.

Who May Participate

E-filing of Michigan returns is available to all electronic filers who are accepted into the IRS e-file program and who transmit returns to an IRS Service Center. The IRS mandates preparers filing 11 or more income tax returns to e-file those returns, with minor exceptions. Michigan would expect any preparer e-filing federal returns to also e-file the Michigan returns.

Application Process

To participate, applicants must first apply to the IRS and be accepted. Individuals must register with IRS e-Services and create a new (or revised) IRS e-file application. Individuals can contact e-Help toll-free at 1-866-255-0654 for assistance with the IRS e-file application or if unable to register for e-Services.

Publication 3112 IRS e-file Application and Participation specifies the application process and requirements for federal participation. The definitions used by the IRS of the various categories of electronic filers, EROs, transmitters, or software developers also apply for Michigan e-filing purposes.

Upon acceptance, the IRS Service Center assigns an Electronic Filer Identification Number (EFIN) and, if applicable, an Electronic Transmitter Identification Number (ETIN) to the applicant.

After receiving the federal acceptance information, applicants are automatically accepted into the Michigan e-file program.

IRS regulations require paid tax preparers to use Preparer Tax Identification Numbers (PTINs) for all tax returns and refund claims. Visit the IRS Web site at www.irs.gov for more information.

Acceptance Process

Treasury may conduct a suitability check on applicants who have been accepted in the Fed/State e-file program. Participation in the program may be denied if a company is not registered to conduct business in Michigan, or if there is an outstanding tax liability with Michigan.

Treasury will use the EFIN assigned by the IRS in the Fed/State e-file program. Michigan does not assign any additional identification numbers.

To participate in the e-file program, electronic filers must use software that has successfully completed the IRS and Michigan Participant Acceptance Testing System (PATS). Confirm that the software chosen was approved for Michigan and that the Michigan e-file program is operational before transmitting returns.

A list of approved software companies is available on Treasury's Web site. Tax preparers are not required to file test returns with Michigan.

If, after acceptance, a tax preparer/transmitter or software company has production problems, Treasury reserves the right to disapprove that tax preparer/software company for part or all of the remainder of the filing season.

Michigan Portion of the Electronic Return

The Michigan portion of an electronic return consists of data transmitted electronically and the supporting paper documents. The paper documents contain information that cannot be transmitted electronically.

Electronic Michigan Returns

Michigan **e-file** will support the following forms and schedules:

<u>Form</u>	<u>Title</u>
3174	Direct Deposit of Refund
4013	Resident Tribal Member Annual Sales Tax Credit
4642	Voluntary Contributions Schedule
4884	Pension Schedule*
4973	Pension Continuation Schedule*
4976	Home Heating Credit Claim MI-1040CR-7 Supplemental*
MI-1040	Individual Income Tax Return
MI-1040CR	Homestead Property Tax Credit Claim
MI-1040CR-2	Homestead Property Tax Credit Claim for Veterans and Blind People
MI-1040CR-5	Farmland Preservation Tax Credit Claim
MI-1040CR-7	Home Heating Credit Claim
MI-1040D	Adjustments of Capital Gains and Losses
MI-1040H	Schedule of Apportionment (e-file limited to six occurrences)
MI-2210	Underpayment of Estimated Income Tax
MI-4797	Adjustments of Capital Gains and Losses from Sales of Business Property
MI-8949	Sales and Other Dispositions of Capital Assets
Schedule 1	Additions and Subtractions
Schedule CR-5	Schedule of Taxes and Allocation to Each Agreement
Schedule NR	Nonresident and Part-Year Resident

***New for Tax Year 2012**

Notes: The information from the W-2 and 1099 forms is entered in the software and transmitted with the e-file return. Do not mail W-2 and/or 1099 forms to Treasury. All W-2 and 1099 information, when applicable, is required when submitting a State Standalone return.

When the following forms are included, the MI-1040 **can be filed**, but the forms listed below must be mailed to the address indicated on the form.

<u>Form</u>	<u>Title</u>
4	Application for Extension of Time to File Michigan Tax Returns
MI-1045	Application for Michigan Net Operating Loss Refund

Following is a list of Individual Income Tax Forms, line reference, and filing conditions where attachments are accepted by Michigan. These forms may also be mailed to the address indicated on the form.

<u>Form</u>	<u>Line</u>	<u>Description</u>	<u>File Name</u>	<u>Required</u>
All Forms		Power of Attorney	POA.pdf	No
MI-1040	18	Other State Returns	OtherStateReturn.pdf	No
MI-1040CR	22	Custodial Party End of Year Statement	FEN851.pdf	No
MI-1040CR-2	21			
MI-1040CR-7	24			
All Forms		MI-1310	MI1310.pdf	No

Note: Michigan will accept e-file returns for deceased taxpayers. If a US 1310 is required, that data must be included within the federal folder of the Michigan e-file return. When e-filing on behalf of a single, deceased taxpayer with a balance due federal return and refund Michigan return, the Michigan return can be e-filed and the US 1310 or form MI-1310 (required documents) included as a PDF attachment when supported by the software or mailed to Michigan.

The taxpayer is **not eligible for e-file** for the 2012 tax year if:

1. Filing federal returns or forms excluded in MeF.
2. Filing the MI-1040 and any of the following apply:
 - Prior year return(s) for tax year 2009 or prior
 - Not required to file a U.S. Form 1040 if filing Fed/State
 - Filing Form MI-1040CR-5 with more than 25 agreements
 - Filing Form MI-8949 with more than 18 short-term capital gains/losses or 24 long-term capital gains/losses

- Filing Form MI-4797 with any of the following:
 - More than 16 sales/exchanges of property held over one year
 - More than 13 sales/exchanges of property held one year or less
 - More than 14 gains from disposition of property under Sections 1245, 1250, 1252, 1254, and 1255.

3. Filing the following Michigan forms:

<u>Form</u>	<u>Title</u>
3581	Historic Credit
4534	Venture Capital Deduction
MI-1040X	Amended Michigan Income Tax Return – 2011 and prior
MI-1040X-12	Amended Michigan Income Tax Return – 2012*
MI-1041	Fiduciary Income Tax Return

***New for Tax Year 2012**

4. Reporting flow-through withholding.

Michigan E-file Signature Process

For Fed/State Returns:

Michigan will accept the federal signature (Self-Selected Personal Identification Number (PIN) or Practitioner PIN). Michigan does not require any additional signature documentation. If the taxpayer chooses to complete Form MI-8453, Treasury recommends that the tax preparer retain it for six years. **Do not** mail Form MI-8453 to Treasury.

For State Standalone Returns:

State Standalone returns that are filed by a tax preparer with or without an MI-1040 can be signed using “shared secrets” or Form MI-8453 signature document. The shared secrets consist of SSNs, previous year’s AGI or household income, and the previous year’s tax due or refund amount. If Form MI-8453 is used, the tax preparer may retain a copy of Form MI-8453. The MI-8453 should **not** be mailed to Treasury.

Note: If the return is signed using shared secrets and the return is rejected because the shared secrets do not validate, the taxpayer/tax preparer may correct the shared secrets information and retransmit. There is no limit on how many times the return can be retransmitted in this circumstance.

Volunteer Groups

If the taxpayer is filing a State Standalone return and chooses Form MI-8453 signature method, Form MI-8453 should be mailed to Treasury. Treasury recommends collecting all of Form MI-8453s at the end of the filing season and sending them to Treasury at the address included in the instructions for the form. Volunteer tax preparers may provide taxpayers with their MI-8453 forms and instruct mailing them to Treasury. If located in a permanent facility, volunteer tax preparers may retain Form MI-8453 on file the same as a paid tax preparer.

Refund Returns

Direct Deposit information is part of the electronic record; therefore, a separate 3174 does not have to be completed for e-file. However, remember that the Direct Deposit information for the federal and State returns can be different. This is especially important when the taxpayer has a Refund Anticipation Loan (RAL).

Treasury **cannot** make any changes to Direct Deposit information after the return is transmitted.

For More Information

Visit the federal Web site at www.irs.gov and Michigan Web site at www.MIfastfile.org for more information on the Fed/State e-file Program.

Assistance is available using TTY through the Michigan Relay Service by calling 1-800-649-3777 or 711. Printed material in an alternative format may be obtained by calling (517) 636-4486.

POST-FILING INFORMATION

Mailing Addresses

General income tax correspondence:

Michigan Department of Treasury
Customer Contact Division
P.O. Box 30757
Lansing, MI 48909

Returning State of Michigan warrants:

Michigan Department of Treasury
Receipts Processing Division
P.O. Box 30788
Lansing, MI 48909

Write "Void" across warrant and include a letter of explanation.

Returning a home heating draft for a check:

Michigan Department of Treasury
Customer Contact Division
P.O. Box 30757
Lansing, MI 48909

Write “Void” across draft and include a letter of explanation.

Remind the taxpayer the dollar amount will only be 50 percent of the draft and there will be further reviews of their account.

Refer to the Treasury Web site at www.michigan.gov/treasury for more information.

Amended Returns (MI-1040X or MI-1040X-12)

Form MI-1040X is used to correct or amend information reported on a MI-1040, credit claims, and schedules for the 2011 and prior tax years. Form MI-1040X-12 is used to correct or amend information reported on Form MI-1040, credit claims and schedules for the 2012 tax year. When filing either form, indicate the tax year, give an explanation of the change, and provide any supporting documentation.

If the original return was adjusted by Treasury and the taxpayer disagrees with the adjustments, it is not necessary to file an amended return. Simply respond to the adjustment notice with documentation to support the original claim. Treasury will review the documentation for further adjustment.

Exceptions: When correcting a *Homestead Property Tax Credit* (Form MI-1040CR) and no MI-1040 was filed with the original claim, a MI-1040X is not required. File the MI-1040CR using the corrected figures and write “Amended” at the top of the form.

When correcting a *Home Heating Credit* (Form MI-1040CR-7), file a MI-1040CR-7 and write “Amended” at the top of the form. An amended claim requesting an additional heating credit must be submitted by September 30, following the year of the claim.

When correcting a *Farmland Credit Claim* (Form MI-1040CR-5), file a MI-1040CR-5 and write “Amended” at the top of the form. Submit the amended form along with a description and any documentation needed to explain the change.

An amended return is not required to change an incorrect SSN or incorrect mailing address. Contact Treasury at www.michigan.gov/iit or call (517) 636-4486.

An amended return claiming an additional refund must be filed within four years of the due date of the original return.

SUMMARY OF CHANGES FOR 2012

Tax Rate (annualized)	4.33%
Personal Exemption (annualized)	\$3,763
Special Exemption for Seniors	\$0
Special Exemption for Disabled	\$2,400
Child Care Deduction	\$0
Qualified Disabled Veteran Deduction	\$300
Pension Deduction	
Single Filer	
Born before 1946: private pension limit	\$47,309
Born 1946 through 1952	\$20,000
Born after 1952, pension not deductible	\$0
Jointly Filed	
Born before 1946: private pension limit	\$94,618
Born 1946 through 1952	\$40,000
Born after 1952, pension not deductible	\$0
Senior Interest, Dividend, and Capital Gains	
Single Filer (not available for senior born after 1945)	\$10,545
Jointly Filed (not available for senior born after 1945)	\$21,091

SUMMARY OF CHANGES FOR PRIOR YEARS

	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>
Tax Rate	4.35%	4.35%	4.35%	4.35%
Personal Exemption	\$3,500	\$3,600	\$3,600	\$3,700
Special Exemption	\$2,200	\$2,300	\$2,300	\$2,400
Child Care Deduction	\$600	\$600	\$600	\$600
Qualified Disabled Veteran Deduction	\$250	\$300	\$300	\$300
Pension Deduction				
Single Filer	\$43,440	\$45,120	\$45,120	\$45,842
Jointly Filed	\$88,880	\$90,240	\$90,240	\$91,684
Senior Interest, Dividend, and Capital Gains				
Single Filer	\$9,690	\$10,058	\$10,058	\$10,218
Jointly Filed	\$19,380	\$20,115	\$20,115	\$20,437

FILING REQUIREMENTS

Filing a MI-1040 Return

An individual must file a Michigan return if they were a Michigan resident all or part of the year and filed a federal return. A nonresident of Michigan is required to file a return if all or part of their income was earned in Michigan or was from Michigan sources.

A nonresident or part-year resident must use *Nonresident and Part-Year Resident Schedule* (Schedule NR) to allocate income between Michigan and other states.

Married taxpayers who filed a joint federal return must also file a joint Michigan return. Taxpayers may file either a separate or joint Michigan return if separate federal returns were filed.

Factors to Determine Domicile

A person who is domiciled in Michigan is a Michigan resident. Domicile means the fixed and permanent home to which a person, wherever temporarily located, always intends to return. A person may have several residences, but may only have one domicile.

Domicile, once established, is not lost until there is a concurrence of all the following:

1. The specific intent to abandon the old domicile.
2. The intent to acquire a specific new domicile.
3. Actual physical presence in the new state of domicile. Generally, the domicile of the wife follows that of the husband.

Factors to be considered in determining a taxpayer's residency or domicile include where they keep their most important possessions, house their family, vote, maintain a club or lodge membership, buy automobile licenses, maintain a mailing address and bank, operate a business, or sue for divorce. However, no one of these factors is controlling.

Nonresident Aliens

Nonresident aliens must file a Michigan income tax return if their federal AGI is more than their Michigan exemption allowance. A copy of federal form U.S. 1040NR, including all schedules and worksheets, must be attached to the MI-1040.

Wages or other income received by a nonresident alien working in Michigan are subject to the Michigan income tax as provided for in Michigan Compiled Laws (MCL) 206.110(2). However, due to tax treaty considerations between the U.S. and other countries, wages and other income received by a nonresident alien living and working in Michigan may not be subject to the Michigan income tax if the income is excluded from AGI.

See Federal Publication 901 for information on U.S. tax treaties with other countries.

A nonresident alien must file a U.S. 1040NR. This return reports all income received by the nonresident alien reduced by wages or other income that is exempted by a U.S. tax treaty.

A nonresident alien is not considered to be domiciled in Michigan and, therefore, may not claim a homestead property tax credit.

Taxability of Income Derived Within Indian Country

Where the Tribal Member's Tribe Does Not Have an Implemented Tax Agreement With the State of Michigan

An individual who is a resident of Michigan and has income from Michigan sources is required to file a Michigan income tax return in accordance with MCL 206.315(1). This provision requires every person who is required to file a return under the Internal Revenue Code (IRC) to file a return under the ITA if their AGI is in excess of the personal exemptions allowed under the act.

An exception exists for an enrolled member of a federally recognized Indian Tribe/Band located in Michigan where the member resides within, and the income generating activity occurs within, the member's own Tribe's Indian country (as defined by 18 USC 1151).

Although the State cannot require tribal members to file a Michigan income tax return if all of their income is earned within their own Indian country and they meet the criteria identified below, it is recommended they file returns to avoid possible contact by Treasury based upon State and federal match programs. A return is required from tribal members if any of the Michigan income is earned outside of their Indian country and/or if any of the criteria below is not met.

Income can be deducted on the Michigan return if **all** the following conditions exist:

1. Individual is a member of a federally recognized Indian Tribe or Band.
2. Individual resides within their own Tribe or Band Indian country.
3. Activity creating the income in question occurs within the member's Tribe Indian country.
4. Individual attaches a signed *Certification for Exempt Income By Indian Tribal Member* (Form 3832) with the return (to be supplied by Treasury).

Note: Treasury may require additional documentation to support the above assertions.

The following income is subject to Michigan income tax:

1. Tribal member income earned outside of member's own Tribe Indian country (including income earned within another Tribe's Indian country).
2. For nontribal members or tribal members not meeting the exemption criteria, all Michigan income is taxable whether earned inside Indian country or not.

Where the Resident Tribal Member's Tribe Has an Implemented Tax Agreement With the State of Michigan

Refer to the Frequently Asked Questions or terms of the agreement posted on Treasury's Web site for details on Resident Tribal Member treatment where the member's Tribe has entered into a tax agreement with the State. See Treasury's Web site at www.michigan.gov/taxes. Click on *Income Tax* or *Business Information* on the left side of the screen, then click on *Native American*. If the Tribe has an implemented agreement, it will be posted at this location. If the Tribe is not listed, there is no implemented agreement for that Tribe or its members.

Estimated Income Tax

Annualized tax rate and fourth quarter estimates for 2012

Although the tax rate was reduced to 4.25 percent as of October 1, 2012, the annualized rate is 4.33 percent. Taxpayers should not use the 4.25 percent rate for their fourth quarter estimated payment. Instead, taxpayers should use 4.33 percent, but may reduce their fourth quarter estimate by any overpayment made in the first three quarters as a result of the reduction in the tax rate.

Forms

Personalized 2013 *Estimated Individual Income Tax Vouchers* (Form MI-1040ES) will be mailed to taxpayers (usually in late January or early February) who paid 2012 quarterly individual income tax estimates and did not use a tax preparer. Tax preparers should use their clients' personalized forms whenever possible. The personalized forms help ensure the correct account is credited. **Never photocopy** someone else's personalized forms. Personalized forms are coded with taxpayers' SSNs and are optically scanned. Coded information is machine readable on photocopies and through correction tape and fluid.

Requirements for Filing and Paying

Section 301(1) of the ITA of 1967 states:

"Every person on a calendar year basis, if the person's annual tax can reasonably be expected to exceed the amount withheld under section 351 and the credits allowed under this act by more than \$500.00, shall pay to the department installments of estimated tax under this act on or before April 15, June 15, and September 15 of the person's tax year and January 15 in the following year. Subject to subsection (3), each installment shall be equal to $\frac{1}{4}$ of the taxpayer's estimated tax under this act after first deducting the amount estimated to be withheld under section 351."

Interest is due for each quarter if no payment is made or an underpayment exists. Taxpayers who have previously filed estimated tax payments, *Underpayment of Estimated Income Tax* (Form MI-2210) or were assessed in a prior year for underpayment or failure to file estimates will be assessed penalty as follows:

- 10 percent penalty for underpayment, or
- 25 percent penalty for failure to file estimated tax payments.

Failure to Make Estimated Payments

Use Form MI-2210 to compute the penalty and interest on the underpayment and file with the 2012 return. If estimated payments are due and have not been paid or are underpaid, Treasury will assess penalty and interest not paid by the taxpayer. The assessment will bill interest on the amount of tax that was due for **each quarter**. An individual may avoid all or part of the penalty and interest if any of the following apply:

1. An individual was not required to file a tax return for 2011.
2. The individual was required to file a return for 2011 but had no tax liability.
3. The amount of tax withheld plus estimated tax payments equal at least:
 - 90 percent of the tax due for 2012, or
 - 100 percent of the tax due for 2011 (110 percent of total tax if your 2011 AGI is more than \$150,000 for single filers or married, filing jointly; or more than \$75,000 for married filing separately).
4. If income is not received evenly during the year, an individual may annualize their income to determine the quarterly estimated payments. (See 2012 MI-2210 for instructions.)

Annual Estimated Tax Returns

An individual may file an annual return of estimated tax rather than quarterly returns. To use this option, the taxpayer must file the 2013 first quarter MI-1040ES and pay the total estimated annual tax by April 15, 2013.

Overpayments Credited Forward to Year 2013

Treasury will reduce a claimed credit forward to the next year if the return is adjusted. The individual will be notified of the adjustment and the reduction of the credit forward. It is the individual's responsibility to make up any deficiency that may result.

Seafarers, Farmers, and Commercial Fishermen

A seafarer, farmer, or commercial fisherman who receives at least two-thirds of their gross income from seafaring, farming, or fishing may file a Michigan annual return of estimated tax no later than January 15, and remit the entire amount of estimated tax with the return. This payment date may be ignored if the seafarer, farmer, or fisherman files their income tax return and pays the entire amount of tax due by March 1.

If a joint return is filed, the seafarer, farmer, or fisherman must also consider their spouse's gross income in determining if at least two-thirds of gross income is from seafaring, farming, or fishing.

Wages earned and other income received by seafarers domiciled in Michigan and sailing the Great Lakes or other waterways are subject to the Michigan income tax as provided for in MCL 206.110(1). As such, seafarers must file an annual Michigan income tax return. Section 46 USCS 11108 precludes the states from withholding state income tax on seafarers' wages; however, it does not prohibit states from subjecting seafarers' wages to state income tax.

EXEMPTIONS

The number of exemptions that may be claimed is the number of allowable federal personal and dependency exemptions plus Michigan special exemptions. As of 2012, no additional special exemptions are available for seniors or for unemployment compensation. In addition, the child care deduction is no longer available.

The following chart lists the Michigan exemption allowance.

<u>Tax Year</u>	<u>Based on Federal Exemptions</u>	<u>Michigan Special Exemptions</u>
2008	3,500	2,200
2009	3,600	2,300
2010	3,600	2,300
2011	3,700	2,400
2012	3,763	2,400 (See exemption limits below)

Definitions of Michigan Special Exemptions

Beginning in 2012, special exemptions are no longer available for seniors or for individuals receiving greater than 50 percent of their AGI from unemployment compensation. Only taxpayers who have one or more of the impairments described below may claim a special exemption.

Deaf. An individual whose hearing is totally impaired or whose hearing, with or without amplification, is so seriously impaired that the primary means of receiving spoken language is through other sensory input, including but not limited to lip reading, sign language, finger spelling, or reading. [Reference: MCL 206.30(3)(a) and 393.502]

Paraplegic. An individual who has paralysis of the lower half of the body. *[Reference: MCL 206.30(3)(a)]*

Quadriplegic. An individual who has paralysis of both arms and legs. *[Reference: MCL 206.30(3)(a)]*

Hemiplegic. An individual who has paralysis of one side of their body. *[Reference: MCL 206.30(3)(a)]*

Blind. An individual who has a permanent impairment of both eyes of the following status: central visual acuity of 20/200 or less in the better eye with corrective glasses, or central visual acuity of more than 20/200 if there is a field defect in which the peripheral field has contracted to such an extent that the widest diameter of visual field subtends an angular distance of not greater than 20 degrees in the better eye. *[Reference: MCL 206.30(3)(a) and 206.504(1)]*

Totally and Permanently Disabled. An individual who is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death, or which has lasted or can be expected to last for a continuous period of not less than 12 months.

Support for this exemption is the receipt of any of the following types of income:

- Social Security Disability benefits
- Supplemental Security Income (SSI) disability benefits
- Veterans' Administration disability retirement payments.

A taxpayer who does not receive any of the above income may be required to furnish a physician's statement to certify total and permanent disability. *[Reference MCL 206.30(3)(a), 206.522(4) and 42 U.S.C. 416]*

Note: A taxpayer who is age 66 or older may not claim an exemption for totally and permanently disabled.

Example 1: Jacob is 66, but before he turned age 66 he received Social Security Disability for being totally and permanently disabled. Assuming Jacob is not deaf, blind, or para/quadri/hemiplegic, Jacob's exemption allowance is limited to the personal exemption. He is not eligible to receive a special exemption because the normal retirement age of individuals born between 1943 and 1954 is 66. Since Jacob has reached normal retirement age, he is no longer receiving disability income but is instead considered a retired senior.

Note: Although Jacob's condition did not change when he reached the age of 66, he may no longer claim an exemption for being totally and permanently disabled.

Example 2: Judy is 67 and is deaf and blind. She received Social Security Disability until the age of 66. Judy's exemption allowance for 2012 would be computed as follows:

Federal Exemption (one x \$3,763)	\$3,763
Michigan Special Exemptions (one for blind or deaf)	<u>2,400</u>
Total Exemption Allowance	\$6,163

Part-Year and Nonresident

The exemption allowance for a part-year resident or a nonresident is prorated based on the taxpayer's Michigan income subject to tax divided by total AGI.

For a couple filing a joint return, if one spouse is a full-year resident and the other is a part-year resident or nonresident, the full-year resident is entitled to one full \$3,763 exemption. The part-year resident or nonresident must prorate the \$3,763 exemption in the ratio of their Michigan income subject to tax to their AGI from all sources. Exemptions for dependents must be prorated in the ratio of combined (both spouses') Michigan income subject to tax to combined AGI from all sources.

Example: Jack and Jill were married June 30, 2012. Jill has two dependent children under 19. Jill worked and lived in Georgia prior to their marriage. She continued to work after moving to Michigan in June 2012. Her interest was received equally throughout the year. Jack was a Michigan resident for all of 2012. Their income was as follows:

	Jack	Jill
Wages	\$56,000	\$25,000
Interest	<u>3,000</u>	<u>5,000</u>
Total AGI	\$59,000	\$30,000

The exemption allowance is computed as follows:

Jack was a Michigan resident all year and is entitled to a \$3,763 exemption allowance. Jill earned wages of \$15,000 in Georgia, and 50 percent of her interest income is allocated to Georgia.

Michigan income (divided by) total income	<u>\$12,500</u> \$30,000 = 42%
42% Michigan sourced income x \$3,763 =	\$1,580

Dependents - Combined Michigan source to all sources

Combined Michigan income	<u>\$71,500</u>		
(divided by) combined total income	\$89,000	=	80%

80% Michigan source income x \$7,526 = \$6,021

Total exemption allowance for 2012 joint Michigan income tax return is:

Jack	\$3,763
Jill	1,580
Dependents	<u>6,021</u>
Total	\$11,364

Claimed as a Dependent

An individual cannot claim a personal exemption if another taxpayer (usually a parent) can claim a dependency exemption for that person. This is true even when the individual is not actually claimed as a dependent on the other's return. However, an individual who is eligible to be claimed as a dependent on someone else's return and has an AGI of **\$1,500 or less** is entitled to a **refund** of all Michigan tax withheld. An individual who is eligible to be claimed as a dependent on someone else's return and has an AGI of **more than \$1,500** is entitled to a \$1,500 deduction.

A dependent who may not claim a personal exemption may still claim one or more of the special exemptions.

Example 1: Carlton (age 16 and can be claimed as a dependent on his parents' return) earned \$6,500 during 2012. He is considered deaf, as defined in MCL 206.30(3)(a) and MCL 393.502. His AGI is \$6,500 and his Michigan income tax withholding is \$165. Carlton's Michigan income tax liability is computed as follows:

AGI	\$6,500
Less: Deduction	(1,500)
Michigan Special Exemption	<u>(2,400)</u>
Taxable Income	\$2,600
x Tax Rate	x <u>0.0433</u>
Michigan Income Tax (Rounded)	\$ 113
Less Michigan Income Tax Withheld	<u>(165)</u>
Refund	\$ 52

Example 2: Terri is 17 and can be claimed as a dependent by her parents. Terri's AGI for 2012 is \$1,250 and her Michigan income tax withholding is \$80. Terri's Michigan income tax liability is computed as follows:

AGI	\$1,250
Less: Deduction	<u>(1,500)</u>
Taxable Income	0
x Tax Rate	x 0.0433
Michigan Income Tax (Rounded)	\$ 0
Less Michigan Income Tax Withheld	<u>(80)</u>
Refund	\$ 80

MICHIGAN INCOME TAX TREATMENT OF CHILD'S UNEARNED INCOME

IRC Section 1(g)7 provides for an election that allows parents to include unearned income of a child on the parents' return when the child: (1) is under the age of 19 or the age of 24 if a full-time student whose earned income does not exceed half of their own support; (2) has no income other than interest, dividends, and/or capital gain distributions; (3) has gross income less than \$9,500; and (4) has no estimated payment or withholding made on behalf of the child.

If the parents take the IRC Section 1(g)7 election, the amount of the child's unearned income in the parents' AGI is subject to Michigan income tax. The amount must also be included in total household resources when computing the property tax and home heating credits.

ADJUSTMENTS TO ARRIVE AT MICHIGAN TAXABLE INCOME

The following is a list of common additions and subtractions made on the Michigan income tax return.

Additions

Interest and dividend income from non-Michigan municipal obligations (add this income even if it comes through a fund, partnership, S corporation, estate, or trust)

Capital gain adjustments (from Michigan column of *Adjustments of Capital Gains and Losses* (Form MI-1040D) or *Adjustments of Capital Gains and Losses From Sales of Business Property* (Form MI-4797))

Losses from a business or property located in another state

Losses from the disposal of U.S. obligations to the extent used in arriving at AGI

Taxes on or measured by income (e.g., deduction for self employment tax)

An unqualified withdrawal from education savings accounts under the Michigan Education Savings Program (MESP) Act if the amount was not included in AGI

Amount of federal Net Operating Loss (NOL) deduction (NOL carryforward) used to reduce AGI

Refund received from a Michigan Education Trust (MET) contract.

Subtractions

Income from U.S. government obligations reduced by any expenses in carrying the obligation used in arriving at AGI

Income from a business or property located in another state

Compensation and retirement benefits received for services in the U.S. Armed Forces to the extent included in AGI. (Do not deduct compensation received from the U.S. Public Health Service.)

Pension/Retirement benefits received from the service in the Michigan National Guard*

Capital gain adjustments (from federal column of MI-1040D or MI-4797)

Retirement/pension benefits. (Caution: these benefits have been limited and are discussed in detail in a separate section on Retirement and Pension Benefits)

Dividend/interest/capital gains deduction for senior citizens (*Caution:* this subtraction is no longer available for individuals born after 1945)

Michigan state and local income tax refunds to the extent included in AGI

Property tax credit to the extent included in AGI

Social Security benefits to the extent included in AGI

Income earned while a resident of a Renaissance Zone that was certified or renewed before January 1, 2012

Pension benefits under the Railroad Retirement Act Tier 1 are taxable as Social Security on the federal return and should be subtracted as Social Security benefits to the extent included in AGI

Contributions made after October 1, 2000, to the MESP, not to exceed \$5,000 for a single return or \$10,000 for a joint return per year

The amount of an advance payment under a MET contract during the tax year.

*This provision is contained in pending legislation (SB 409) as of the date of this publication and is expected to be enacted. Please visit www.mileg.org for additional information and updates.

Items Not Allowed as Subtractions

Itemized deductions from federal Schedule A

Unemployment benefits included in AGI

Sick pay, disability benefits, and wage continuation benefits paid to a taxpayer by their employer or by an insurance company under contract with the employer

Distributions from deferred compensation

Lottery winnings won on January 1, 1989 or later

Out-of-state gambling winnings taxed by another state (a credit for taxes paid may be available).

MISCELLANEOUS DEDUCTIONS

Income From Oil and Gas Production

Beginning in 2012, the subtraction of gross oil and gas income from AGI as set forth in *Elenbaas v Department of Treasury*, 235 Mich App 372 (1999) is repealed. Deduct the gross oil and gas income from AGI and add back the related expenses to AGI.

RENAISSANCE ZONES

The Michigan Renaissance Zone Act, PA 376 of 1996, permitted the designation of specific regions in Michigan as Renaissance Zones. The Michigan Economic Development Corporation (MEDC) administers the Renaissance Zone program and conducts the zone selection process.

Generally, an individual living in or a business located and conducting business activities in a Renaissance Zone certified or renewed before January 1, 2012 will receive an exemption, deduction, or credit from the following State and local taxes:

- | | |
|--------------|--|
| Individuals: | Michigan Income Tax |
| | Property Tax (except debt mills) |
| | City Income Tax (if applicable) |
| | Utility Users Tax (Detroit only) |
| Businesses: | Property Tax (except debt mills) |
| | Portion of Michigan Business Tax and City Income Tax |
| | attributable to business activity in the zone. |

However, no deduction or credit will be allowed if the taxpayer is delinquent in any taxes covered in the Renaissance Zone Act.

Note: A designated zone may be located within the boundaries of a city or county, but there are no established zones that include an entire city or county. Contact the local authority to determine if you or your client lives within the boundaries of a zone.

Residents of a Renaissance Zone are eligible for a deduction on the Michigan income tax return after meeting the Zone residency requirement of at least 183 consecutive days. Persons whose gross income exceeds \$1 million for the tax year are **not** eligible for the deduction. The taxpayer can deduct most income earned and received while a resident of the Zone. Form MI-1040 must be filed to claim the deduction. Once an individual has completed the 183-day residency requirement in a Zone, that individual should file a revised *Employee's Michigan Withholding Exemption Certificate* (Form MI-W4) to claim exemption from Michigan income tax withholding. The employer should stop Michigan income tax withholding upon receipt of a revised MI-W4 and must forward a copy of the MI-W4 to Treasury.

Zones began phasing out in 2006. The tax exemption is phased out in 25 percent increments during the zone's final three years of existence. Check with the client's local unit of government to determine if the phase-out has begun. The credit is reduced as follows:

- 25 percent for the tax year that is two years before the final year of the designation as a renaissance zone.
- 50 percent for the tax year immediately preceding the final year of the designation as a renaissance zone.
- 75 percent for the tax year that is the final year of the designation as a renaissance zone.

For information regarding the specific zones, visit the MEDC Web site at <http://medc.michigan.org/services/sitedevelopment/renzone/>. For tax questions relating to the zones, contact Treasury at (517) 636-4280.

PENSION AND RETIREMENT BENEFITS

For purposes of this section, the term "pension" will include pension and retirement benefits.

A subtraction may be allowed on the Michigan return for qualifying distributions from pension plans. Pension plans include private and public employer plans, and individual accounts governed by various sections of the IRC.

The pension subtraction involves two steps. **First**, the pension distribution must meet certain requirements to be characterized as a qualified distribution. **Second**, a qualified distribution may be subject to a dollar limitation on the amount of the subtraction. Beginning in 2012, the benefit may be further limited based on the date of birth of the retiree on a single return or the date of birth of the oldest spouse on a joint return.

Step 1: Qualified Distribution Requirements

Employer plans and individual plans each have rules for receiving pension distributions. For a pension distribution to qualify for the Michigan subtraction it must comply with the specific distribution rules under its plan.

Employer Plans

Employer plans are created by private companies and by public entities. The employer plan establishes the rules that govern retirement age and the pension formula for its employees. For both public and private employer plans, an employee must retire under the provisions of the plan, the pension benefits must be paid from a retirement trust fund, and the payment must be made to either the employee or the surviving spouse. (Payments made to the surviving spouse are only deductible if the employee qualified for the subtraction at the time of death.)

Although traditional employer plans are defined contribution and defined benefit plans, many employers are now using 401(k) or 403(b) plans that incorporate employee match provisions.

Distributions from a 401(k) or 403(b) plan are qualified distributions to the extent that they are attributable to the employer's contributions or employee's contributions that were mandated by the plan. An employee's contribution required by the plan to elicit an employer match is considered mandated. Amounts distributed from a 401(k) or 403(b) plan that allows the employee to set the amount of compensation to be deferred and does not prescribe retirement age or years of service **do not** qualify as pension benefits.

Individual Plans

Individuals can create their own pension plans. To qualify for the Michigan pension subtraction, the distributions must meet the requirements set forth in the relevant section of the IRC.

- **Individual Retirement Account IRC 408 Distribution Requirements.**

1. 59½ or older, or
2. Disability, or
3. Death - Distributions after the death of the participant may only be subtracted by a surviving spouse, and only if the distributions qualified as a subtraction for the participant at the time of death; or
4. Series of equal periodic payments made for life under IRC Section 72(t)(2)(iii)(iv).

Distributions from a Roth Individual Retirement Account (IRA) are not included in AGI and are not subtractable on the Michigan return. Roth IRAs are treated in more detail later in the text.

- **Senior Citizen Annuity IRC 72 Distribution Requirements.**

1. Received from a retirement annuity policy, and
2. For life, and
3. To a senior citizen.

For purposes of the retirement annuity subtraction, a senior citizen is defined in MCL 206.514(1) as an “individual . . . who is 65 years of age or older at the close of the tax year. The term also includes the unremarried surviving spouse of a person who was 65 years of age or older at the time of death.”

- **401(k), 403(b), and 457 Plans.** If all the contributions are made by the employee or if the employee makes contributions that are **not** matched by the employer, any distributions attributable to the employee contributions will not qualify for the pension subtraction.
- **Keogh or HR 10 Plans for the Self-Employed.** Distributions are subject to the same general rules for other retirement plans, usually not made until a participant separates from service, the plan is discontinued, or the participant reaches age 59½.

The following distributions do not qualify for the pension subtraction:

1. Deferred compensation plans that allow the employee to set the amount of compensation to be deferred and do not prescribe retirement age or years of service
2. Commercial Annuity Policies (unless the payments are made for life to a senior citizen)
3. Premature separation, withdrawal, or discontinuance of a plan prior to the earliest date the recipient could have retired under the provisions of the plan
4. Payments received as an incentive to retire early unless the distributions are from a pension trust
5. Eligible distributions received by a beneficiary of the decedent except the surviving spouse.

Step 2: Dollar Limitations on Pension Subtractions

Once it has been determined that a pension distribution has met the requirements of a qualified distribution set forth in Step 1, the next step is to determine if there are any dollar limitations on the amount of the Michigan pension subtraction.

For 2012 and future tax years, new limitations on pension deductions have been added based on the year of birth of the retiree who is a single filer or on the year of birth of the oldest spouse for joint filers. The sections that follow first discuss dollar limitations based on year of birth. After the date of birth limitations have been discussed, the private pension limitations will be reviewed. Beginning in 2012, maximum private pension limitations only apply to taxpayers who were born before 1946. For taxpayers who were born during or after 1946, public/private pension limitations do not apply because new lower limits have been placed on the pension deduction for these taxpayers.

Pension Limitations Based on Date of Birth

MCL 206.30(8) defines “retirement or pension benefits.” MCL 206.30(9) provides limitations to the deduction, depending upon the birth year of the retiree, as well as filing status and marital status. Retirees are divided into three tiers based on date of birth of the taxpayer or the date of the oldest spouse on a joint return.

Tier 1: For a taxpayer born before 1946, there are no additional restrictions or limitations to the deduction allowed under MCL 206.30(1)(f).

Tier 2: For a taxpayer born in 1946 through 1952, the maximum pension deduction is \$20,000 for a single return or \$40,000 for a joint return. At age 67, the deduction is no longer restricted to pensions but can be applied to all income. This general deduction is sometimes referred to as a “standard deduction” because it is applied against all income.

If a taxpayer receives a pension from a governmental agency that was not covered by the federal Social Security Act (SSA), the “uncovered” taxpayer may deduct \$35,000 on a single return and \$55,000 on a joint return (\$70,000 on a joint return if both spouses were “uncovered”).*

Tier 3: For a taxpayer born after 1952, there is no pension deduction in 2012. However, for some taxpayers in Tier 3, at age 62 there is limited deduction if a taxpayer receives a pension from a governmental agency that was not covered by the federal SSA. The “uncovered” taxpayer, who is at least 62, may deduct \$15,000 or \$30,000 if both spouses were “uncovered.”*

All taxpayers in Tier 3 are eligible for the \$20,000 single/\$40,000 joint standard deduction upon reaching age 67.

*This provision is contained in pending legislation (SB 409) as of the date of this publication and is expected to be enacted. Please visit www.mileg.org for additional information and updates.

INCOME TAX CHANGES FOR RETIREMENT BENEFITS EFFECTIVE FOR TAX YEAR 2012

Taxpayers born before 1946 (Tier 1) No change in current law	Taxpayers born 1946 through 1952 (Tier 2) Before the taxpayer reaches age 67	Taxpayers born after 1952 (Tier 3) Before the taxpayer reaches age 67
<ul style="list-style-type: none"> • Social Security is exempt. • Senior citizen subtraction for interest, dividends, and capital gains up to \$10,545 for single filers and \$21,091 for joint filers. • Public pensions exempt. • For 2012 private pensions, subtract up to \$47,309 for single filers and \$94,618 for joint filers. 	<ul style="list-style-type: none"> • Social Security is exempt. • Railroad pension is exempt. • Military/Michigan National Guard* pension is exempt. • Not eligible for the senior citizen subtraction for interest, dividends, and capital gains. • Public and private pension limited subtraction of \$20,000 for single filers or \$40,000 for joint filers. • Pensions from governmental agencies not covered by the Social Security Act. \$35,000 for single filer, \$55,000 for joint filers, or \$70,000 for joint filers if both spouses worked for an “uncovered” agency.* 	<ul style="list-style-type: none"> • Social Security is exempt. • Railroad pension is exempt. • Military/Michigan National Guard* pension is exempt. • Not eligible for the senior citizen subtraction for interest, dividends, and capital gains. • Not eligible for public or private pension subtraction. • At age 62, pensions from governmental agencies not covered by the Social Security Act \$15,000 for single or joint filer or \$30,000 for joint filers if both spouses worked for an “uncovered” agency.*
	After the taxpayer reaches Age 67 (will first occur in 2013)	After the taxpayer reaches Age 67 (will first occur in 2020)
	<ul style="list-style-type: none"> • Social Security is exempt. • Railroad pension is exempt (see below). • Military/Michigan National Guard* pension is exempt (see below). • Not eligible for the senior citizen subtraction for interest, dividends, and capital gains. • Subtraction against all income of \$20,000 for single filers and \$40,000 for joint filers. <p>Note: Not eligible for this income subtraction if choosing to claim a Military/Michigan National Guard* or Tier 2 railroad pension exemption.</p>	<ul style="list-style-type: none"> • Not eligible for the senior citizen subtraction for interest, dividends, and capital gains. • Not eligible for public or private pension subtraction. • Income exemption election: <ul style="list-style-type: none"> – Elect exemption against all income of \$20,000 for single filers or \$40,000 for joint filer, OR Note: No exemption for Social Security, Military/Michigan National Guard*, or railroad retirement. No personal exemptions – Elect to exempt Social Security, Military/Michigan National Guard* and railroad pension. May claim personal exemptions.

*This provision is contained in pending legislation (SB 409) as of the date of this publication and is expected to be enacted. Please visit www.mileg.org for additional information and updates.

Unlimited Public Pension Subtraction

Applies only to retirees born before 1946 (Tier 1).

Michigan and Federal Public Pensions

Federal or Michigan public pensions are no longer totally exempt. The amount that may be deducted depends on the year of birth for a retiree who is single filer or on the year of birth of the oldest spouse for joint filers.

Public pensions include benefits received from the federal civil service, State of Michigan, political subdivisions of Michigan, military return, and railroad retirement. If the requirements of the plans under Step 1 are met, these distributions may be deductible depending on the age of the filers.

Public Pensions: Railroad Retirement and Pension Benefits

The taxable amount of Railroad Pension income included in AGI may be subtracted on the Michigan return. (Portions of a Railroad Pension are treated as Social Security (SS) on the federal return and should be subtracted as SS benefits to the extent included in AGI.)

Public Pensions From Other States

Michigan allows a pension subtraction for public pensions earned in other states by Tier 1 retirees if the other state permits a deduction, or exemption of a retirement or pension benefit received from a Michigan public retirement system. To the extent included in AGI, Michigan allows the **greater of:**

- \$47,309 for a single return or \$94,618 for a joint return for the 2012 tax year (private pension limits)

OR

- Amount allowed as a deduction or exemption by the other state to its residents on public pensions received from Michigan.

For most public pensions from other states, the Michigan subtraction for Tier 1 retirees will be limited to the private pension limits of \$47,309 or \$94,618. However, there are 14 states that allow a complete exemption for public pensions earned in Michigan and one state that has a higher pension deduction than Michigan's private pension limits.

The following states allow a 100 percent deduction or exemption for their residents who receive Michigan public pensions. Therefore, **for Tier 1 retirees (those born before 1946)**, the full amount of the pension distribution included in AGI is subtractable on the Michigan return for **public** pensions received by Michigan residents from the following states:

Alaska	New Hampshire
Florida	Pennsylvania
Hawaii	South Dakota
Illinois	Tennessee
Massachusetts	Texas
Mississippi	Washington
Nevada	Wyoming

For all other public pensions from states other than the 14 with complete exemptions, the Michigan private pension limits will be the maximum subtraction allowed for Tier 1 retirees. For all other retirees the pension limitations are based solely on date of birth and there is no difference between a private and a public pension.

Combined Public and Private Pension

Applies only to retirees born before 1946 (Tier 1)

An individual with a pension from both public and private sources must reduce the maximum allowable subtraction for the private pension by any public pension distribution.

Private Pensions

Private pensions include employer plans and individual plans such as IRAs and senior citizen annuities. The maximum subtraction allowed for a Tier 1 retiree with a private pension is adjusted annually by the percentage increase in the U.S. Consumer Price Index. The maximum deduction for the 2012 tax year is \$47,309 on a single return and \$94,618 for a joint return.

The following table outlines the annual maximum pension deductions:

<u>Tax Year</u>	<u>Single Return</u>	<u>Joint Return</u>
2008	43,440	86,880
2009	45,120	90,240
2010	45,120	90,240
2011	45,842	91,684
2012	47,309*	94,618*

***Only applies to retirees born before 1946 (Tier 1).
For all other retirees lower limits apply.**

Pension Subtraction Examples

Example 1: Combined Public and Private Pension distributions.

Sam is retired and single and born before 1946. He has a State of Michigan pension of \$33,000 and a private pension of \$15,000. His total pension deduction for 2012 is determined as follows:

Maximum Private Pension Deduction	\$47,309
Less: Public Pension	<u>-33,000</u>
Allowable Private Pension Subtraction	\$ 14,309
Sam's total pension subtraction is:	
Public	\$33,000
Private	14,309
Total	\$47,309

If Sam's public pension was more than \$47,309, he would not be able to subtract any of his private pension.

Example 2: Employer and Employee contributions to a 401(k) plan.

Stuart's employer established a 401(k) plan for its employees. The plan provides for a 50 percent employer match of employee contributions up to the maximum employer match of 3 percent of the employee's salary. The plan also allows the employees to make additional unmatched contributions up to the annual percentage rate allowed by the IRC. In 2012, Stuart retired under the provisions of the retirement plan at age 60. At the time of his retirement, Stuart received an annual statement from the 401(k) plan showing total contributions of \$400,000, of which \$100,000 were employer contributions. Stuart took a distribution of \$25,000 in 2012, the year he retired.

Since the plan includes unmatched employee contributions, Stuart must determine what amount of the \$25,000 distribution is attributed to the unmatched contributions. The plan called for a 50 percent employer match; therefore, \$200,000 of the employee contributions was required to elicit \$100,000 employer matching contributions. The remaining account balance of \$100,000 is unmatched employee contributions. The deductible amount of the 2012 distribution is determined as follows:

$$\$100,000/\$400,000 \times \$25,000 = \$6,250 \text{ (distribution attributed to unmatched distribution)}$$

\$25,000 - \$6,250 = \$18,750 (Maximum allowable pension subtraction. Actual subtraction may be further limited based on the date of birth of the retiree.)

Rollovers of Roth IRAs

A Roth IRA is treated differently than a traditional IRA under the IRC. Under a traditional IRA, the contributions are excluded from AGI but the distributions are taxed. Under a Roth IRA the reverse occurs; the contributions are taxed and the distributions are not.

Contributions to a Roth IRA are not tax exempt and are subject to the Michigan income tax to the extent the contributions are included in federal AGI.

A rollover from a regular IRA to a Roth IRA is subject to Michigan income tax to the extent the rollover is included in federal AGI. However, if an individual is 59½ when the rollover occurs, the individual may deduct the rollover as a pension deduction within the statutory limits for deducting pension income.

Also, a rollover from a regular IRA to a Roth IRA is subject to Michigan income tax for a taxpayer moving into and domiciled in Michigan to the extent the rollover is included in AGI. Conversely, a taxpayer moving from Michigan to another state is not taxed on the amount of a rollover from a regular IRA to a Roth IRA during the years the taxpayer is not domiciled in Michigan.

A qualified distribution from a Roth IRA is not subject to Michigan income tax because the distribution is not included in federal AGI.

A rollover from a regular IRA to a Roth IRA is included in total household resources in the year the income is included in the taxpayer's federal AGI. Tax year 2003 was the first year a qualified or tax-free distribution could be made from a Roth IRA. The amount of a qualified distribution in excess of a taxpayer's contributions (rollover or regular contributions) must be included in total household resources. A nonqualified or taxable distribution from a Roth IRA must be included in total household resources to the extent it is included in a taxpayer's federal AGI. Investment losses from the liquidation of a Roth IRA are not allowed in total household resources.

<p>Note: All pension income must be included in total household resources except for any nondeductible contributions that are included in the pension distribution and any amounts that are rolled over into other plans. Generally, only the taxable portion of the pension benefits from the 1099-R is included in total household resources.</p>
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2012 Pension and Retirement Subtraction Table for Tier 1 Retirees

The 2012 deductible retirement and pension benefits are limited to the lesser of the amount included in AGI or the amounts shown below.

<u>Source of Retirement Benefits</u>	<u>Single</u>	<u>Joint</u>
U.S. Civil Service	Amount included in AGI	Amount included in AGI
State of Michigan	Amount included in AGI	Amount included in AGI
Michigan political subdivisions	Amount included in AGI	Amount included in AGI
Private	\$47,309	\$94,618
Public pensions (from other states)	\$47,309 or reciprocal limit, whichever is greater	\$94,618 or reciprocal limit, whichever is greater
Qualified senior citizen retirement annuities	\$47,309	\$94,618
Public and private	Limited to public pension or \$47,309, whichever is greater (cannot exceed actual qualified distributions received).	Limited to public pension or \$94,618, whichever is greater (cannot exceed actual qualified distributions received).

1099 R Distribution Codes

Recipients of a pension distribution receive form 1099R. There is a box on form 1099R titled “Distribution code(s).” Look in the “Distribution code(s)” box for the number that describes the condition under which the pension or retirement benefit was paid.

1099R Dist. Code	<u>Description</u>	Is the condition eligible for Michigan tax exemption? (<u>Dollar and date of birth limits may still apply.</u>)
1	Early distribution, no known exception	No
2	Early distribution, exception applies	No, unless: <ul style="list-style-type: none"> • Part of a series of substantially equal periodic payments made for the life of the employee or the joint lives of the employee and employee’s beneficiary. • Early retirement under the terms of the plan.
3	Disability	Yes
4	Death	<ul style="list-style-type: none"> • Yes, for surviving spouse only and only if the decedent would have also qualified for a normal distribution under Distribution Code 7 at the time of death. This may be subject to limitations based on the year of birth of the decedent. • No, for all other beneficiaries. • No, if paid as a death benefit payment made by an employer but not made as part of a pension, profit-sharing, or retirement plan.
5	Prohibited transaction	No
6	Section 1035 exchange: tax-free exchange of life insurance, endowment insurance, and annuity contracts	No
7	Normal distribution: normal distribution from a plan; distribution from a traditional IRA if the participant is at least 59½; Roth conversion if the participant is at least age 59½; or distribution from a life insurance, annuity, or endowment contract	Yes
8	Taxable excess contribution plus earnings/excess deferrals (and/or earnings)	No
9	Cost of current life insurance protection	No

DEFERRED COMPENSATION

Distributions received from deferred compensation plans which allow the employee to set the amount of compensation to be deferred and do not prescribe retirement age or years of service are treated as ordinary income. Deferred compensation distributions are usually **not** considered pension income and may **not** be subtracted on the Michigan return.

Federal law, 4 USC 114, prohibits a state from taxing certain deferred compensation distributions received by a nonresident after December 31, 1995. Therefore, nonresidents are no longer subject to Michigan income tax on distributions from deferred compensation plans as defined in IRC Sections 401(k), 457, and 3121(v)(2)(c) for payments received after December 31, 1995.

INTEREST, DIVIDENDS, AND CAPITAL GAINS DEDUCTION FOR SENIOR CITIZENS BORN BEFORE 1946

Senior citizens born before 1946 may take a deduction for interest, dividends, and capital gains up to \$10,545 for a single return and \$21,091 for a joint return for the 2012 tax year. The deduction will be adjusted by the percent increase in the U.S. Consumer Price Index for future years. This maximum deduction must be reduced by the amount of deduction taken for pension and retirement income.

Example: Step 1: James and Joanne are retired senior citizens, James was born before 1946. They file a joint income tax return. A partial listing of their income is as follows:

Pension Income	\$ 4,000
Capital Gains	12,000
Dividend Income	1,800
Interest Income	3,800

Step 2: Calculation of interest, dividend, and capital gains deduction:

Maximum Deduction	\$21,091
Less: Pension Subtraction	<u>4,000</u>
Maximum Allowable Deduction	\$17,091

Step 3: Total interest, dividends, and capital gains = \$17,600

Step 4: Use the **lesser** of the total interest, dividends, and capital gains (\$17,600) or the maximum allowable deduction (\$17,091).

Step 5: The interest, dividends, and capital gains deduction for James and Joanne is **\$17,091**.

Note: The term “senior citizen” as used in this section, refers to a person 65 years of age or older or an unremarried surviving spouse of an individual who was 65 years of age or older at the time of death. Beginning in 2012, this deduction is available only to taxpayers born before 1946 or the surviving spouse.

529 EDUCATION PLANS

Michigan Education Savings Program

The MESP is administered by Treasury and managed by TIAA-CREF. To open an education savings account, an individual must enter into an agreement with the program manager. The maximum account balance limit to any one beneficiary account cannot exceed \$235,000.

Distributions from the account must be used to pay qualified higher education expenses incurred after the account is established. A nonqualified distribution will be subject to a penalty of 10 percent of the distribution if no federal penalty is imposed on the nonqualified withdrawal.

A deduction may be taken on the Michigan income tax return for contributions made to the MESP on or after October 1, 2000. The maximum deduction is \$5,000 for a single filer (\$10,000 for a jointly filed return). The amount deducted includes total contributions made to the plan less qualified withdrawals made during the tax year. A taxpayer must add to federal AGI any nonqualified withdrawal from the MESP in the year of the withdrawal.

Interest earned on contributions made to an MESP account may be deducted to the extent included in AGI. The beneficiary of the MESP account may deduct qualified withdrawals to the extent included in AGI.

For more information on the MESP, contact MESP at 1-877-861-MESP or www.misaves.com.

Michigan Education Trust



The MET allows parents, grandparents, and others to prepurchase undergraduate in-state and in-district tuition for a child at any Michigan public college, university, junior college, or community college.

Payments made under an advance payment contract in a MET during the tax year are deductible to the extent they are included in federal AGI on a purchaser's Michigan income tax return. The \$25 application fee may also be subtracted on the Michigan return. Interest payments made on loans to finance the contract are not deductible. MET contracts are only set up in specified enrollment periods.

Beginning with the 2002 tax year, earnings on the qualified distributions are tax-free on the beneficiary's federal and State income tax returns. A nonqualified distribution is subject to federal and State income tax.

For more information or contract materials on MET, contact MET at 1-800-MET-4-KID at treasMET@michigan.gov or at www.michigan.gov/setwithmet.

Coverdell Educational Savings Account (formerly Educational IRA)

The Coverdell Educational Savings Account (Coverdell ESA) is structured as a trust or a custodial account for the purpose of paying educational expenses of a designated beneficiary and follows the same general rules as other IRAs.

The contributions made to a Coverdell ESA are not tax deductible. Beginning January 1, 2002, the contributions are limited to \$2,000 a year.

The distributions from a Coverdell ESA are tax-free if they do not exceed the beneficiary's qualified educational expenses to an approved educational institution. An approved institution is any accredited postsecondary educational institution offering credit towards an associates, bachelors, graduate level, or professional degree.

Any investment earnings will accrue tax-deferred or tax-free. However, any distribution that is included in AGI is taxable in Michigan.

NONRESIDENTS' TAXABLE INCOME

The following income of nonresidents is subject to the Michigan income tax:

1. Salary, wages, commissions, and other personal service income for work performed in Michigan.
2. Income allocable or apportionable to Michigan, including portfolio income, from partnerships, S corporations, and limited liability companies having business activity in Michigan, or business or farm income from a sole proprietorship or farm located in Michigan. Significant changes to the apportionment of business income have occurred as a result of legislative changes taking effect in 2012 and as a result of several decisions by the Court of Appeals addressing the application of the unitary business principle to tiered flow-through entities. (See flow-through entities for more information.)
3. Rent and royalty income from real and tangible personal property located in Michigan.
4. Capital gains/losses from the sale or exchange of real or tangible personal property located in Michigan.
5. Patent or copyright royalties if the patent or copyright is used in Michigan or has a commercial domicile in Michigan.
6. Michigan lottery, raffle, bingo, and charitable gaming winnings.
7. Casino winnings and winnings from pari-mutuel wagering at licensed horse racing meetings.
8. Distributable net income received from a trust attributable to Michigan, including business income and gain from property located in Michigan.

Michigan has **reciprocal agreements** with **Illinois, Indiana, Kentucky, Minnesota, Ohio, and Wisconsin** that exempt nonresidents from income taxes imposed by each state on salaries, wages, and other employee compensation. Business income and gambling income are not subject to these reciprocal agreements. Business income is subject to the allocation and apportionment provisions of the Income Tax Act (ITA).

Withholding for Nonresidents

PA 21 of 2003 requires nonresidents to pay Michigan income taxes on winnings from casinos and pari-mutuel wagering at licensed horse racing meetings. The act is effective for amounts won beginning October 1, 2003.

The act applies to winnings from casinos regulated under the Michigan Gaming Control and Revenue Act, tribal casinos where gaming is conducted under the federal Indian Gaming and Regulatory Act, and horse racing licensed under the Horse Racing Act of 1995.

PA 22 of 2003 amended the ITA to extend the withholding requirements that are currently imposed on employers so that they apply to:

1. Distributable income from flow-through entities earned by nonresident members
2. Winnings of nonresidents reportable under federal casino law by casinos licensed under the Michigan Gaming Control and Revenue Act, and
3. Winnings of nonresidents reportable under the federal law by race meeting licensees and track licensees operating under the Horse Racing law of 1995.

Beginning in 2012, the withholding requirements for flow-through entities with individual nonresident members were reenacted by the legislature as MCL 206.703. The withholding and reporting obligations of a flow-through entity are discussed in detail in the Flow-Through Withholding chapter of this publication. A flow-through entity is required to furnish to a nonresident individual member information about the taxable Michigan portion of the member's distributive share and the amount of withholding in some manner, such as in the supplemental information to the federal schedule K-1 that the member receives from the flow-through entity.

FLOW-THROUGH ENTITY DISTRIBUTION OF INCOME AND LOSSES

Business income derived from business activity in Michigan is subject to income tax. Business income can be sourced to a sole proprietorship or to a flow-through entity. Income received from a “C corporation” is not business income if it is received as wages or as dividends. Income from the sale of a partnership interest is generally not business income and is attributable to the state of residence of the owner. Modifications to the apportionment of business income have occurred because of a legislative change requiring the use of only the sales factor beginning in 2012. Changes to the apportionment of business income have also occurred as result of Court of Appeals decisions that apply the unitary business principle retroactively to require combined apportionment of tiered flow-through entities if the entities operate on a unitary basis. The requirement of combined apportionment is discussed in detail under a separate heading on apportionment of unitary businesses.

Income flowing through to a shareholder of an S corporation, a partner of a partnership, a member of a limited liability company, or the owner of any other flow-through entity is business income and is subject to the allocation and apportionment provisions of the Michigan Income Tax Act. The taxpayer’s distributive share of such income and losses shall be allocated or apportioned to the state where the business activity takes place using the three-factor apportionment formula for 2011 and earlier years and on only the sales factor beginning in 2012. The apportionment is computed on *Schedule of Apportionment* (Form MI-1040H).

Income allocated or apportioned to Michigan is taxable to Michigan. Income not allocated or apportioned to Michigan may be claimed as a subtraction from AGI. Conversely, losses not allocated or apportioned to Michigan must be added to AGI.

Portfolio income is business income and is subject to allocation or apportionment. Portfolio income includes interest income, dividend income, royalty income, and net short-term and long-term capital gain (loss) reported on the federal Schedule D. Resident or nonresident individual taxpayers having portfolio income from a multistate partnership, S corporation, or other flow-through entity must apportion this income using the apportionment formula as computed on MI-1040H.

A nonresident member of any flow-through entity doing business in Michigan must file a Michigan return to report their distributive income from the flow-through entity. The income is taxable even if it is not actually distributed to the member.

When filing Form MI-1040H, it should be noted that the computation of the apportionment percentage is not the same for Individual Income Tax (IIT) as for Michigan Business Tax (MBT) or Corporate Income Tax (CIT). When computing the sales factor, throwback sales for individual income tax follow Public Law (PL) 86-272 standards. Also, foreign sales can be in the numerator for IIT purposes. The IIT standard for determining if the taxpayer is taxable in another state uses the PL 86-272 nexus criteria. In general, a taxpayer’s business must have property in another state or activity that goes beyond solicitation of sales to be taxable in the other state.

An S corporation is permitted to own a qualified subchapter S subsidiary (QSub). The term includes any domestic corporation that qualifies as an S corporation and is 100 percent owned by an S corporation parent, which elects to treat it as a QSub. The assets, liabilities, and items of income, deduction, and credit of the QSub are treated as those of the parent S corporation.

Composite Individual Income Tax Return for Nonresident Partners/Shareholders/Members

Partnerships, S corporations, limited liability companies, and other flow-through entities can file a composite return for nonresident partners/shareholders/members. The entity must have two or more nonresident partners/shareholders/members who participate on the composite return. Flow-through entities may not file a composite return on behalf of C-corporation members.

The entity must withhold income tax on the taxable distributive share of net profits reported on the federal schedule K-1 even if the members do not receive a distribution of income. The flow-through entities must register with Treasury and file quarterly withholding returns. The withholding requirements for income tax do not affect any obligation that the entities or their members may have under the MBT Act.

The participants can be other flow-through entities as well as individuals. In addition, individual participants who have other Michigan income may not subtract the income reported on the composite return but may claim a credit for their share of the tax paid on a composite return when filing an individual income tax return.

APPORTIONMENT OF TIERED FLOW-THROUGH ENTITIES UNDER THE UNITARY BUSINESS PRINCIPLE

In addition to the change in the apportionment to a single sales factor starting in 2012, the Michigan Court of Appeals has issued decisions in three published cases that significantly change the way business income is apportioned for tiered flow-through entities. The change required by the Court of Appeals applies to 2012 and also applies to all earlier open years. Amended returns are required if a flow-through entity's business income is subject to combined apportionment.

The due process and commerce clauses of the U.S. Constitution impose limitations on a state's power to tax activity beyond its borders. However, when an entity operates in more than one state, the task of assigning income among the various states becomes difficult. The Supreme Court permits states to tax a business on an apportionable share of the multistate business based on the proportion of activity that took place in the taxing state. This is known as the unitary business principle. A unitary business is one that has centralized management or some other flow of value between its various operations. Flow of value can be from economies of scale in purchasing resources, or functional integration through shared service such as payroll or strategic planning.

Treasury previously applied the unitary business principle to each discrete legal entity's business operations. This single entity apportionment approach has been overturned by the Michigan Court of Appeals. The court has ruled that for flow-through entities in a tiered structure, all of the entities must use combined apportionment if the entities operate in a unitary manner. (See *Preston v. Department of Treasury*, 292 Mich App 728, NW 2d, 2011 WL 2090901; appeal denied 490 Mich 893, 804 NW 2d 324; *Wheeler et al. v. Department of Treasury*, court of appeals 302251, 302259, 302261, and 302262, May 15, 2012.)

Combined apportionment means that if a flow-through entity operates solely in another state or foreign country and another flow-through entity that is part of the same tiered structure has some or all of its activity in Michigan, then the income of all tiers must be combined and apportioned using the combined factors of all flow-through entities. Prior to the court of appeals ruling, a flow-through entity with no activity in Michigan would have no part of its income apportioned to Michigan.

Tiered flow-through entities will be considered unitary if they share centralized management, even if the management is from an outside source that is otherwise independent of the tiered structure (*Preston*), or if they share an employee services. Unlike the CIT, there is no statutory right to eliminate intercompany transactions and there is no "waters edge."

The court of appeals has also ruled that the unitary business principle does not require combined apportionment for flow-through entities that are held directly by a taxpayer (brother-sister companies). *Malpass et al. v. Michigan Department of Treasury*, NW 2d, 295 Mich App 263, 2011 WL 6061351 Mich App.

MI-1040D - ADJUSTMENTS OF CAPITAL GAINS AND LOSSES

The purpose of *Adjustments of Capital Gains and Losses* (Form MI-1040D) is to exclude from Michigan taxable income gains and losses that are not subject to tax by Michigan. Michigan has had IIT since October 1, 1967. If a taxpayer sells property that they owned prior to that date, only that portion of the gain attributable to the time Michigan has had an income tax can be taxed. Similarly, if the gain was attributable to another state and therefore not subject to Michigan tax, it cannot be included in Michigan taxable income. The MI-1040D adds in the Michigan gain and subtracts out the federal gain so the taxpayer is only taxed on the Michigan portion. If the MI-1040D computes to a loss, the federal loss is added back in the same manner as an out-of-state loss and the Michigan loss is subtracted.

Form MI-1040D for the adjustment of **capital gains and losses** must be used if any of the following are true:

1. Taxpayer disposes of assets acquired prior to October 1, 1967, and elects to exclude gains or losses under Section 271.

To apportion under Section 271:

Multiply gain or loss by number of months property was held after September 30, 1967. Then divide the result by the total number of months held.

2. Taxpayer has gains or losses from the sale or exchange of U.S. obligations that cannot be taxed by Michigan.
3. Taxpayer has gains or losses from property subject to the allocation and apportionment provisions.

Example: Robert reported the following capital gains on his federal Schedule D:

From sale of stock	\$ 9,800
From sale of real property in Phoenix, Arizona	<u>5,800</u>
Total Schedule D capital gain	\$15,600

After preparing the MI-1040D, the \$15,600 total capital gain is reported as a subtraction from AGI on the MI-1040, and the \$9,800 capital gain on the sale of stock is reported as an addition to AGI on the MI-1040. This removes the \$5,800 gain from the sale of real property in Phoenix, Arizona from Michigan taxable income.

NET OPERATING LOSS (NOL) CARRYBACK AND CARRYFORWARD

MCL Sections 206.30(1)(m) and (n) were enacted by legislative amendment in 1987 to provide an NOL deduction for Michigan income tax purposes. Several court cases (*Preston v. Department of Treasury*, 190 Mich App 4941, 476 NW 2d 455 (1991), and *Beznos v. Department of Treasury*, 224 Mich App 717; 569 NW 2d 908 (1997)) have clarified the income tax treatment of the Michigan NOL and NOL deduction. In *Preston*, the Michigan Court of Appeals ruled that a taxpayer could have a Michigan NOL in the absence of a corresponding federal NOL. In *Beznos*, the Court held that the Michigan NOL deduction was **not** limited to the smaller of the federal NOL deduction or federal modified taxable income. In so ruling, the Court stated that the Michigan NOL and NOL deduction must be computed without federal itemized deductions.

As a result, Treasury calculates the Michigan NOL and NOL deduction independently of the federal NOL and NOL deduction. The Michigan NOL calculation is computed by applying the NOL provisions of IRC Section 172 to only income, losses, and deductions allocated and apportioned to Michigan under Chapter 3 of the ITA. Further, the Michigan NOL is computed without regard to federal itemized deductions in the year of the loss, or income and losses from oil and gas production that is subject to Michigan Severance Tax. The Michigan NOL so computed may then be subtracted in full on the Michigan return in the year to which it is properly carried.

For tax years beginning before 2012, the allowed NOL deduction used to reduce household income may not exceed federal modified taxable income, or the federal NOL deduction, whichever is smaller. The inclusion of the allowed NOL deduction in household income may be used to increase the amount of the homestead property tax credit and the farmland preservation tax credit. The NOL carryback cannot be used to claim a home heating credit.

Beginning in 2012, “**household income**” is replaced by “**total household resources.**” Neither the federal nor the Michigan NOL may be used to reduce total household resources for purpose of the home heating credit or the property tax credit.

Michigan follows the federal provisions in determining the eligible carryback or carryforward years. Generally, the Michigan NOL amount may be carried back two years. For 2008 and 2009, many taxpayers may qualify to use a three-, four-, or five-year carryback period in the same manner as provided in the IRC. Any unused balance may be carried forward 20 years.

Note: Any federal domestic activities production deduction under IRC 199 must be added back in calculating a Michigan NOL and also removed from the carryback or carryforward year.

NOL Frequently Asked Questions

1. Q. If a return with an NOL is filed after the four-year statute of limitations for claiming a refund has expired, does the taxpayer lose the benefit of the NOL?
 - A. The taxpayer cannot file a claim for a refund for any years that are beyond the four-year statute of limitations. (Exception: If the loss year (NOL year) return is filed within four years of the due date, the NOL may be carried back to a year that is otherwise outside of the statute of limitations and a refund will be issued.) However, the taxpayer must use the Michigan NOL to the extent of Michigan income subject to tax in the closed years to determine the amount that can be carried forward to years that are filed within the four-year statute of limitations and before carrying forward the balance of any remaining NOL.
2. Q. Can a taxpayer create a Michigan NOL if there is no corresponding federal NOL?
 - A. Yes, based on the Appeals Court decision in *Arthur Preston v Michigan Department of Treasury*. Complete *Application for Net Operating Loss Refund* (Form MI-1045) to determine the amount of the Michigan NOL. This may occur when a taxpayer has income from other states or income from oil and gas production that is subject to Severance Tax.

3. Q. What are the implications on an NOL carryback/forward when the filing status of an individual changes (e.g., joint to separate or single)?

A. **Year of NOL**

Year of Carryback/forward

Joint NOL Single or separate return filed - determine each individual's share of the joint NOL and apply their share to their separate or single returns.

Married,
Filing Separate Joint return filed - apply NOL to the joint return.

Single Joint return filed - separate individuals' income and deductions and apply NOL to the individual sustaining an NOL as a single individual.

4. Q. Can there be a difference in the amount of a Michigan NOL and a Federal NOL?

A. Yes, the Michigan NOL is computed without considering federal itemized deductions as well as income and losses attributable to other states and income and losses from oil and gas production.

5. Q. Can an NOL carryback/forward be used to reduce household income? (Applies to years before 2012 and when computing the Farmland Preservation Tax Credit.)

A. Yes, to the extent of a taxpayer's federal modified taxable income. Remember, the federal NOL deduction is **not** subject to apportionment for household income purposes. Beginning in 2012, "total household resources" replaces "household income." An NOL cannot be used to reduce "total household resources."

6. Q. Must Form MI-1045 be filed or can Form MI-1040X be filed?

A. If carrying the loss back, Form MI-1045 must be filed. A copy of the original Form MI-1045 must also be submitted in years when losses are carried forward.

7. Q. What should be included in income reported on page 1 of the MI-1045?

A. Page 1 should reflect the Michigan portion of federal AGI. It should not include income or losses from other states and it should not include gross income from oil and gas royalties subject to Michigan Severance Tax. In addition, beginning in 2012, do not include the expenses related to the gross income from oil and gas royalties subject to Michigan Severance Tax.

8. Q. Should a State or local refund be included even though it is not taxable to Michigan?

A. Yes, any state or local refund included in federal AGI should be included on page 1 of Form MI-1045. It is used in the computation of the MI-1045.

9. Q. Should pension income or SSI be reported even though it may not be taxable on the Michigan return?

A. Yes, any portion of pension or SSI included in federal AGI for the loss year must be included in the MI-1045 computation.
10. Q. What must be sent to verify a taxpayer is a Day Trader?

A. Day Traders must include a copy of an approved 475(f) election from the IRS.
11. Q. Is the NOL amount allowed as a deduction to household income for years before 2012 and for the Farmland Preservation Credit the same as the amount computed on page 1 of the MI-1045?

A. No, the NOL deduction allowed in household income is limited to federal modified taxable income or the federal NOL, whichever is less.
12. Q. What documentation is necessary to support an NOL claim?

A. A copy of the federal return for the loss year, a copy of the completed federal 1045 (if applicable), the state of location for any claimed business losses on federal schedules, a copy of any attachments indicated on federal schedules, K-1's, *Adjustments of Gains and Losses From Sales of Business Property* (MI-4797), MI-1040D, and Schedule H must be submitted to verify any apportionments.
13. Q. How is a carryforward documented in a succeeding tax year?

A. A copy of the original MI-1045 prepared for the year the loss was created and a copy of the worksheet showing how the loss has been used in previous and succeeding years should always be submitted to verify the claimed carryforward.

Tips for Filing

1. When completing Form MI-1045, exclude income and losses from other states in Part 1.
2. The main concerns when reviewing a return with an NOL deduction are determining if:
 - The apportionment provisions of the ITA have been complied with, and
 - For years before 2012 and for the Farmland Preservation Tax Credit, the NOL deduction has been correctly limited to federal modified taxable income in the schedule of household income on the refundable credit claims (e.g., homestead property tax credit). Beginning in 2012, the federal NOL is not part of total household resources.
3. To claim a refund from a carryback of a Michigan NOL, complete and file Form MI-1045. If any of the refundable credits are affected by the NOL carryback, a copy of the revised credit claim form must be attached. Form MI-1040X (amended return) is not required to be attached to Form MI-1045.

4. To expedite processing, include copies of pages 1 and 2 of a taxpayer's federal income tax return and all supporting federal tax schedules when an NOL deduction is claimed for both the year of the loss and the year it is carried to. If the information is not attached, Treasury may write to the taxpayer and request copies of these schedules.
5. When listing an NOL deduction, specifically identify the amount. Many times a notation is made, such as miscellaneous deductions, which includes other items (e.g., jury duty, directors' fees, etc.) that makes it impossible to determine what amount the taxpayer is claiming as an NOL deduction. Beginning in 2012, a Michigan NOL deduction is reported separately on the Schedule 1 and is not included on the miscellaneous subtractions line with these other items.
6. Be sure to attach a calculation of the amount of all NOLs included in the NOL deduction claimed on the Michigan return.
7. For years before 2012, enter allowable NOL deduction on line 25 on the property tax form MI-1040CR as other adjustments to income and write "NOL" on the line.
8. A taxpayer may create a federal NOL when AGI is greater than zero, which will result in a Michigan NOL deduction in the pre-2012 schedule of household income only and for the Farmland Preservation Credit. Itemized deductions may not be used to create a Michigan NOL deduction for Michigan taxable income purposes.
9. Casualty losses, employee business expenses, and other itemized deductions classified as business expenses for federal NOL purposes may create or contribute to a Michigan NOL deduction for pre-2012 household income purposes only and for the Farmland Preservation Credit. Itemized deductions are not part of the calculation of a Michigan NOL. When calculating pre-2012 household income with a federal NOL deduction created in whole or in part by federal itemized deductions, include federal Schedule A and any related schedules (e.g., federal *Casualties and Thefts* (Form 4684)) for the year in which the NOL occurred.

GAMBLING INCOME

Income from gambling activities from Indian or privately held casino's games of chance, horse racing, lottery winnings, etc., is subject to Michigan income tax to the extent the winnings are included in federal AGI.

Gambling losses may be deducted as a federal Schedule A itemized deduction to the extent of gambling winnings on the federal income tax return. However, itemized deductions are deductions from AGI and, therefore, are not included in federal AGI. Because the computation of Michigan taxable income begins with federal AGI, gambling losses cannot reduce Michigan taxable income.

Casual gamblers may not net their gains and losses throughout the year and report only the net amount of gain or loss for the year. Each gambling session stands alone and cannot be netted with other gambling sessions or games. A casual gambler who plays slot machines may net gains and losses at the end of each slot machine session. Casual gamblers must provide proof of the slot machine sessions according to standards set forth in the IRS Publication 529.

For tax years before 2012, certain cash prizes or merchandise won in Michigan may be deducted in determining Michigan taxable income. To qualify for the deduction, the prize must have been awarded by a Michigan licensed bingo game, millionaire party, or charity game conducted in conformity with the Traxler-McCauley-Bowman Bingo Act, PA 382 of 1972, as amended (MCL 432.101 through MCL 432.120). The amount of the deduction is limited to the amount of the prize included in federal AGI and is limited to years before 2012.

Michigan residents who are casual gamblers cannot subtract out-of-state gambling winnings from AGI. However, a credit against the tax may be available.

MILITARY PAY

Pay received by members of the U.S. armed forces is not subject to Michigan income tax. Military pay includes:

- Active duty pay and military retirement pay, including Michigan National Guard pension/retirement benefits
- Reserve duty pay
- Michigan National Guard pay **only for the following:**
 - Weeknight and regular weekend drills
 - Summer camp
 - Pay received for riot duty **only if nationalized by the President of the U.S.**
 - Public Health Officers pay only for those assigned to the Coast Guard or who are **nonresidents of Michigan.**
 - Pension/Retirement benefits (beginning in 2012).*

The W-2 form will show if individual's pay is active duty military pay. If the second set of digits of the employer identification number begins with 997, 998, or 999, the pay is military pay. Military pay may be subtracted on the Michigan return to the extent included in federal AGI.

Military pay does **not** include:

- W-2 forms from an Officer's Open Mess or similar establishment
- W-2 forms from the military showing an employer number identifying a civilian employee
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*This provision is contained in pending legislation (SB 409) as of the date of this publication and is expected to be enacted. Please visit www.mileg.org for additional information and updates.

- Wages paid to employees of the United States Property and Fiscal Office (USPFO)
- National Guard pay for the following:
 - Riot duty when called to duty by the Governor (paid by the State)
 - Full-time employment for which the taxpayer received a W-2 from the State.
- Resident Public Health Officers (employees of Health and Human Services) for other than the Coast Guard.

Note: Residency of military personnel and Public Health Officers remains with the state from which they entered the service unless they have filed a declaration with the service to change it.

The Military Spouses Relief Act was signed into law on November 11, 2009, effective for tax years beginning on or after January 1, 2009. It may affect the State income tax filing requirements for a spouse of an individual in the military.

Under the Act, the spouse of an individual in the military is a nonresident of a state and consequently not subject to that state's taxation if:

- The service member is present in that state due to military orders
- The spouse is in that state solely to accompany the service member
- The spouse maintains a domicile in another state.

Therefore, a military spouse who is a Michigan resident and plans to return to Michigan as their permanent home should include income earned in the other state on their Michigan Income Tax return. A Michigan military spouse may not claim a credit for the income taxes paid to another state. The military spouse must file a nonresident return with the other state to obtain a refund of taxes paid to that state.

PRINCIPAL RESIDENCE EXEMPTION

The Principal Residence Exemption Program (PRE), formerly known as the Exemption Program, allows homeowners an exemption from their local School Operating Millage (it lowers their property tax bill). In accordance with PA 237 of 1994, homeowners who occupy their property as their principal residence may be exempt from up to 18 mills.

To claim a PRE, a homeowner must file a *Principal Residence Exemption Affidavit* (Form 2368) with the township or city assessor. A homeowner who occupies a property on or before June 1 and submits Form 2368 to the local tax collecting unit on or before June 1 may qualify for a PRE beginning with the summer tax levy. A homeowner who occupies a property as a principal residence at any time from June 2 to November 1 and submits Form 2368 to the local tax collecting unit on or before November 1 may qualify for a Principal Residence Exemption beginning with the winter tax levy.

This program is separate from the Homestead Property Tax Credit, which is filed annually with Michigan income tax returns.

Principal Residence Exemption Records Review

In many cases, the local unit of government performs administrative audits of the PRE records. PA 105 of 2003 allows county treasurers and equalization directors who have elected to “opt in” with Treasury to perform administrative audits of exemptions within their counties. Treasury performs administrative reviews of records for counties that don’t conduct their own audits. In addition, Treasury may choose to audit “opt in” counties.

Periodically, Treasury may contact the homeowner to request information to verify that the property under review was the principal residence for the years in question.

Common reasons for Treasury to request more information are:

- Failure to rescind an exemption when the property is sold (*Request to Rescind Principal Residence Exemption* (Form 2602)).
- The property in question was not a principal residence during the years in question.
- The homeowner is filing annual income tax returns from an address other than the address of the principal residence.

If a letter from Treasury requesting more information is received, it is important to respond in writing. The homeowner’s response must be received within 30 calendar days from the date on the letter. Failure to respond may result in a denial of the exemption.

Verifying Documentation

Factors to be considered in determining taxpayers’ domiciles include where they keep their most important possessions, house their family, vote, maintain club and lodge memberships, buy automobile licenses, maintain a mailing address and bank, operate a business, or sue for divorce. However, no one of these factors is controlling.

The documentation submitted must show that the property was the homeowner’s principal residence for the year(s) in question. Some examples of verifying documentation are:

- Copy of driver’s license with property address
- Copy of voter’s registration record
- Copy of a cancelled check listing the property address. Black out any information other than the address and the date the check was written.
- Copy of a bank statement, charge account statement, medical billing, etc. Only the portion identifying the address and date need be submitted.

- Copy of the income tax return indicating the mailing address
- Copy of an insurance policy. Only the portion identifying address and date need be submitted.

If the taxpayer never owned the property or if the information on the letter is incorrect, make corrections on the letter and return it to Treasury.

Conditional Rescission of Principal Residence Exemption

In accordance with PA 96 of 2008, property owners may be allowed to receive a PRE on their current property and on previously exempted property simultaneously if the previously exempted principal residence is (all must apply):

- Not occupied
- For sale
- Not leased
- Not used for any business or commercial purposes.

The extra exemption may be allowed for up to three years and is requested by submitting *Conditional Rescission of Principal Residence Exemption* (Form 4640) with the assessor for the city or township in which the property is located on or before May 1 of the year of the claim. Form 4640 must be filed annually on or before December 31 to verify to the assessor that the property for which the principal exemption is retained still meets all the above requirements. The owner of the property must be eligible for and claim an exemption for his or her new current principal residence. A person renting an apartment is not eligible for a PRE. A person who moves to another state would also not qualify for the PRE.

Foreclosure Entity Conditional Rescission of a Principal Residence Exemption

In accordance with PA 114 of 2012, a land contract vendor, bank, credit union, or other lending institution may retain a PRE on property if the following conditions are met:

- Must be a land contract vendor, bank, credit union, or other lending institution
- Own the property as a result of a foreclosure
- Property must have been subject to a PRE immediately preceding the foreclosure
- Not occupied
- For sale
- Not leased to any person other than the person who claimed the PRE immediately preceding the foreclosure
- Not used for any business or commercial purpose

- Must pay to the tax-collecting unit an amount equal to the amount of taxes that the foreclosure entity would have paid if the property were not subject to a PRE and must pay an administration fee equal to the property tax administration fee imposed under Section 44 of the General Property Tax Act.

The extra exemption may be allowed for up to three years and is requested by submitting *Foreclosure Entity Conditional Rescission of a Principal Residence Exemption* (Form 4983) with the assessor for the city or township in which the property is located on or before June 1 (beginning with the summer tax levy) or November 1 (beginning with the winter tax levy) of the first year of the claim. Form 4983 must be filed annually on or before December 31 to verify to the assessor that the property for which the principal exemption is retained still meets all the above requirements.

Forms for Principal Residence Exemption

Forms are available on Treasury's Web site at www.michigan.gov/PRE.

NONREFUNDABLE CREDITS

Beginning in 2012, the following credits **are no longer available**:

- City Income Tax Credit
- Public Contribution Credit
- Community Foundation Credit
- Homeless Shelter/Food Bank Credit
- College Tuition and Fees Credit
- Vehicle Donation Credit
- Individual or Family Development Account Credit
- Renewable Energy Surcharge Credit

Credit for Income Tax Imposed by Qualified Government Units Outside Michigan

A Michigan resident is allowed a credit for income taxes imposed by another state of the U.S., a political subdivision (city, county, etc.) of another state, the District of Columbia, or a Canadian province. Tax imposed on income that is also subject to Michigan tax may be claimed for the credit. A copy of the other state, city, or county income tax return must be attached.

The credit cannot exceed the smaller of the amount of tax imposed by another state or the percentage of Michigan tax due on salaries, wages, and other income earned and taxed in the other state. Credit is not allowed for taxes paid on income subtracted on the MI-1040.

A Michigan resident who earned wages in a reciprocal state may pay a city or county tax in that state. The city or county income tax paid in that state may be claimed for the credit; however, the state income tax paid to the reciprocal state cannot be claimed. Instead, the Michigan resident should claim a refund from the other state.

A Canadian credit is allowed only if provincial tax was paid. The credit shall be allowed for that portion of the provincial tax not claimed as a credit for United States income tax purposes. Credit is **not** allowed on the Michigan return for that portion of provincial tax that is a carryover from a previous year or that is being carried over to a future year on the federal return.

Historic Preservation Income Tax Credit

For plans approved before 2012, a nonrefundable credit may be taken based on 25 percent of qualified expenditures for the rehabilitation of a historic resource pursuant to a rehabilitation plan.

The claimant must claim the Historic Preservation Credit in the year the project is certified and completed.

Any unused portion of the credit may be carried forward for a maximum of ten years. For tax years beginning after 2008, a taxpayer may elect to receive a refund of 90 percent of the amount of the credit that exceeds their tax liability instead of carrying the excess forward for projects for which a certificate of completed rehabilitation was issued after 2008 and the credit amount was less than \$250,000.

The rehabilitation plan and the completed rehabilitation of the historic resource must be certified by the State Historic Preservation Office.

REFUNDABLE CREDITS

New for 2012

Beginning in 2012 the following refundable credits are no longer available:

- Energy Efficient Qualified Home Improvement Credit
- Stillbirth Credit
- Adoption Credit

The homestead property tax credit has been changed in three major ways. “Household Income” has been replaced by “total household resources” which is calculated without certain net losses or federal NOLs. In addition, senior claimants with income over \$21,000 will have their credit reduced on a sliding scale. Once the senior claimant’s total household resources reaches \$30,001, their credit will be reduced to 60 percent. Finally, the threshold for phase-out of the credit has changed. Beginning in 2012, all claimants will lose 10 percent of their credit once total household resources reach \$41,001 and another 10 percent for each \$1,000 of total household resources in excess of \$41,001.

Total Household Resources

Beginning in 2012, the home heating credit and the homestead property tax credit require the computation of total household resources. Total household resources are defined in MCL 206.508(4) as “all income received by all persons of a household in a tax year while members of a household,” increased by the following deductions from federal gross income:

- A. Any net business loss after netting all business income and loss
- B. Any net rental or royalty loss
- C. Any carryback or carryforward of a net operating loss as defined in Section 172(b)(2) of the internal revenue code.

MCL 206.510 defines income as “. . . federal adjusted gross income plus income specifically excluded or exempt from the computation of federal adjusted gross income.”

Items specifically excluded or exempt from the computation of AGI are generally income that will not be subject to tax in the year actually or constructively received or in a subsequent taxable year under the IRC or by federal laws other than the IRC. Excluded or exempt income includes, but is not limited to, income described in IRC Sections 101 through 134, exempt interest dividends, foreign income exclusion, etc.

Following is a **partial list** of excluded or exempt income that must be included in a claimant’s total household resources:

- 1. SS, SSI, or railroad retirement benefits
- 2. Child support
- 3. Workers’ compensation
- 4. Veterans’ disability compensation and pension benefits
- 5. Family Independence Program (FIP) assistance and Department of Human Services (DHS) benefits (do not include Food Assistance Program benefits)
- 6. Nontaxable sick pay or long-term disability benefits
- 7. Lump sum distribution that has been deducted from federal gross income
- 8. Gains realized on sale of principal residence, even if exempt from tax
- 9. Awards, prizes, lottery, bingo, and gambling winnings over \$300
- 10. Farmland preservation tax credit (if not included in farm income on line 16)
- 11. Amounts received for minor children or other dependent adults who live with claimant
- 12. Inheritance
- 13. Compensation for damages to character or for personal injury or sickness
- 14. Proceeds of a life insurance policy paid on the death of the insured
- 15. Death benefits paid by or on behalf of an employer
- 16. Minister’s housing allowance
- 17. Scholarships, stipends, grants, or GI bill benefits
- 18. Reimbursement from dependent care and/or medical care spending accounts
- 19. Value over \$300 in gifts of cash, merchandise, or expenses paid on claimant’s behalf (rent, taxes, utilities, food, medical care, etc.)
- 20. State Disability Assistance (SDA) and State Family Assistance (SFA)
- 21. Repatriate Assistance and Refugee Assistance
- 22. Vendor payments for shelter, heat, and utilities

23. Rollover amount from an IRA to a Roth IRA to the extent included in AGI
24. Foreign earned income exclusion
25. Accumulation distributions received from a trust not previously included in AGI.

Items not in total household resource (**partial list**):

1. Minor child's income
2. Loan proceeds
3. Refunds of State and local income tax
4. Homestead property tax or home heating credits
5. Original contributions to pension
6. Stipends received under Foster Grandparent Program
7. Inheritance from spouse
8. Life insurance benefits from a policy on claimant's spouse
9. Nontaxable dividend distributions that represent a return of capital
10. Relief in kind paid by a government unit to a third party
11. Losses on the sale of principal residence.

Adjustments to total household resources:

1. Payments to IRA, Keogh (HR 10), SEP, or SIMPLE plans
2. Student loan interest deduction
3. Health savings account deduction
4. Medical insurance/HMO premiums claimant paid
5. Moving expenses when moving into Michigan
6. Deduction for self-employment tax
7. Self-employment health insurance deduction
8. Forfeited interest penalty for premature withdrawal
9. Alimony paid
10. Educator expenses
11. Tuition and fees deduction.
12. Add back to AGI:
 - Any net business loss after netting all business income and loss
 - Any net rental or royalty loss
 - Any carryback or carryforward of a federal net operating loss.

Total Household Resources Examples:

Example 1: For 2012, Judy has wages of \$29,000, nontaxable child support of \$6,000 and a net loss of \$8,000 for the rental of a second home she owns. The AGI reported on her 2012 federal and Michigan returns is \$21,000, which is the wages of \$29,000, less the rental loss of \$8,000:

Judy's 2012 total household resources is calculated as follows:

AGI	\$21,000
Add back Net Rental Loss	8,000
Child Support	6,000
Total Household Resources	\$35,000

Example 2: For 2012, Bob and Martha have wages of \$26,000, business income of \$10,000 reported on federal Schedule C, a farm loss of \$12,000 reported on Schedule F, and a rental loss of \$4,000 reported on Schedule E. They had no nontaxable income. The AGI reported on their 2012 federal and Michigan return is \$20,000 consisting of the wages of \$26,000, business income of \$10,000, and the farm loss of \$12,000, and the rental loss of \$4,000.

Bob and Martha's 2012 total household resources are calculated as follows:

AGI	\$20,000
Add back Net Business Loss	2,000
Add back Net Rental Loss	4,000
Total Household Resources	\$26,000

Property Tax Credit

An individual may claim a property tax credit if they are a resident of Michigan for at least six months of 2012, rent or own a homestead located in Michigan as their principal residence, and the property is subject to ad valorem property tax or a service fee in lieu of taxes. An individual can have only one principal residence (domicile) at a time and must be the occupant as well as the owner or renter. The maximum credit allowed per claimant cannot exceed \$1,200, regardless of the amount of property taxes levied or rent paid.

Beginning in 2012, major changes were made to eligibility requirements for the property tax credit. As noted above, household income has been replaced with total household resources. Also, senior claimants with income greater than \$21,000 will receive less than 100 percent of the property tax credit based on a sliding scale. Once the senior claimant's total household resources reaches \$30,001, their credit will be reduced to 60 percent. Finally, the phase-out range has been reduced to a loss of 10 percent of the credit once total household resources reaches \$41,001 and an additional 10 percent for each \$1,000 of total household resources in excess of \$41,001. The property tax credit is completely phased-out once total household resources exceed \$50,000.

Additionally, regardless of a claimant's total household resources, a homeowner is not eligible for a homestead property tax credit on their home if their home has a taxable value of more than \$135,000.

Total household resources has three components.

The first component is AGI from the federal return. This consists of wages and other taxable income.

The next component is any nontaxable income a taxpayer receives during the year, such as social security benefits, worker's compensation, or public assistance payments.

The last component is the elimination of any net rental and royalty losses; any net business loss after netting all business income and losses; and any carryback or carryforward of a net operating loss that is included or reported in AGI on the Michigan or federal returns.

Senior Claimants. Senior claimants are entitled to a 100 percent credit if their total household resources are \$21,000 or less. The credit is reduced by four percent once total household resources exceed \$21,000:

<u>Total Household Resources</u>	<u>Reduction Percent</u>
\$21,001 - \$22,000	4%
22,001 - 23,000	8%
23,001 - 24,000	12%
24,001 - 25,000	16%
25,001 - 26,000	20%
26,001 - 27,000	24%
27,001 - 28,000	28%
28,001 - 29,000	32%
29,001 - 30,000	36%
30,001 - above	40%

Senior claimants receive a 60 percent property tax credit for total household resources of \$30,001 to \$41,000. The credit phase-out applies once a claimant's total household resources exceed \$41,000. (See chart on next page.)

Disabled claimants. Claimants who are permanently disabled, paraplegic, hemiplegic, quadriplegic or deaf will receive a 100 percent credit if household resources are \$41,000 or less. The credit phase-out applies once total household resources exceeds \$41,000. (See chart on next page.)

General claimants. General claimants receive a 60 percent property tax credit subject to the credit phase-out once total household resources exceed \$41,000. (See chart on next page.)

Credit phase-out. All claimants are subject to the credit phase-out. The credit is reduced by 10 percent for each \$1,000 of total household resources in excess of \$41,000. [See chart below.]

<u>Total Household Resources</u>	<u>Reduction Percent</u>
\$41,001 - \$42,000	10%
42,001 - 43,000	20%
43,001 - 44,000	30%
44,001 - 45,000	40%
45,001 - 46,000	50%
46,001 - 47,000	60%
47,001 - 48,000	70%
48,001 - 49,000	80%
49,001 - 50,000	90%
50,001 - above	No Credit

Example 1: A senior citizen has total household resources of \$45,000 and property taxes of \$2,500. The property taxes exceed 3.5 percent of total household resources by \$925. The senior citizen's total household resources exceed \$30,000, therefore the credit is reduced from 100 percent to 60 percent or \$555. The phase-out applies and will further reduce the \$555 credit by 40 percent to \$333.

Example 2: A claimant has total household resources of \$48,500 and property taxes of \$4,000. The property taxes exceed 3.5 percent of total household resources by \$2,302. The credit is first reduced to 60 percent or \$1,381. The credit is then limited to \$1,200, the maximum allowed. After the \$1,200 limit is applied, the phase-out of 80 percent further reduces the credit to \$240.

Taxable Value. The property taxes on a homestead with taxable value of more than \$135,000 may not be included in the calculation of the property tax credit. The 2012 tax bills received from the homeowner's local government will state the taxable value. The taxable value cap only applies to the residential portion of land for homeowners with adjacent and contiguous farmland listed on the same tax bill and included in the taxable value on the bill. The taxable value cap does not apply to renters.

Eligible property taxes. The property taxes **levied** on the homestead for 2012 are the only taxes that can be claimed for credit regardless of when the taxes are paid. These include additional taxes assessed or refunded that are attributable to a prior year because of a Michigan Tax Tribunal decision or the reversal of a homestead affidavit denial. Also, collection fees of up to 1 percent of the property taxes and special assessments based on state equalized value and applied to the entire taxing jurisdiction may be included. Beginning in 2003, under the authority of PA 28 of 2003, if the special assessment is for police, fire, or advanced life support, the credit may be taken even if the assessment does not cover the entire taxing jurisdiction. However, these special assessments must be based on the taxable value using a uniform millage rate.

Do not include:

- Penalty and interest on late payments of property tax.
- Delinquent property taxes.
- Delinquent water or sewer bills.
- Property taxes on cottages or second homes.
- Special assessments (for drains, sewers, etc.) that are not based on taxable value and are not applied to the entire taxing jurisdiction.
- 2011 winter taxes paid in 2012.

Michigan homestead property tax credit and principal residence exemption refunds received in 2011 may be taxable on the 2012 federal income tax return. These are refunds of a portion of the property taxes paid. If the taxpayer claimed an itemized deduction for property taxes on a prior federal income tax return, and then received a refund in 2012 from the State or local unit of government for a portion of those taxes, a portion of that refund may need to be included as income on taxpayer's 2012 federal income tax return.

For questions about taxability (for federal tax purposes) of these refunds, call the IRS at 1-800-829-1040.

**Reporting Taxable Value (TV) on
MI-1040CR Homestead Property Tax Credit**

The TV of the property must be reported on the MI-1040CR to process property tax credit claims. To avoid possible refund delays, enter the TV on the proper line. Use the following list to determine the correct TV to report in special circumstances.

1. **If the taxpayer moves during the year**, complete the "Homeowners" section showing the TV for each homestead. If there were more than two homesteads during the year, attach an additional sheet. Property taxes levied on occupied homesteads having TV greater than \$135,000 may not be included in total property taxes claimed to calculate the credit.
2. **If the taxpayer lives in a nursing home and the spouse lives in a homestead**, complete the "Special Housing" section and combine the taxes for both residences on line 10.
3. **If the taxpayer's homestead is assessed at the non-homestead rate**, use the actual TV that is being assessed at the non-homestead rate on line 9.
4. **If the taxpayer lives in service fee housing**, leave line 9 blank. A schedule of explanation need not be attached.
5. **If a portion of the homestead is rented out or used for business**, show the total homestead TV on line 9. Reduce the property taxes by the greater of 20 percent of the gross rent collected or the amount of property taxes claimed as a business deduction on the U.S. 1040. Show the explanation either on the return or an attached schedule.
6. **If the property tax claim includes eligible adjacent and contiguous vacant land**, include on line 9 the sum of the TVs for the homestead and all eligible vacant land.

Special Situations

Farmers

Farmers may include farmland taxes in the property tax credit claim if any of the following conditions apply:

- If agricultural gross receipts are greater than total household resources, all farmland property taxes including taxes on unoccupied farmland are eligible for the credit. However, taxes on farmland that is rented by or leased to another person and is not adjacent or contiguous to taxpayer's home is not eligible for the credit.
- If agricultural gross receipts are less than total household resources and taxpayer has lived in the home more than ten years, the taxes on the home and the adjacent and contiguous farmland are eligible for the property tax credit.
- If agricultural gross receipts are less than total household resources and taxpayer has lived in the home less than ten years, the taxes on the home and five contiguous and adjacent acres of farmland are eligible for the credit.
- If the taxable value of your homestead excluding the taxable value of the unoccupied farmland classified as agricultural exceeds \$135,000, you are not eligible for the homestead property tax credit.

Agricultural Gross Receipts

"Agricultural gross receipts" means income derived from the business of farming. A taxpayer is engaged in the business of farming if they cultivate, operate, or manage a farm for gain or profit. A taxpayer who receives a rental which is based upon farm production is also engaged in the business of farming. However, a taxpayer who receives a fixed rental without reference to production is engaged in the business of farming only if they participate to a material extent in the operation or management of the farm. (*Refer to IRS Reg. 1.175-3.*)

The taxpayer has participated to a material extent in the operation or management of the farm if any one of the following tests are met. (*Refer to IRS Publication No. 225.*)

1. The owner does **three** of the following:
 - Advances, buys, or stands good for at least half the direct costs of producing the crops
 - Furnishes at least half the tools, equipment, and livestock used in producing the crops
 - Periodically advises and consults with the tenant
 - Periodically inspects the production activities.

2. The landowner regularly and frequently makes or takes an important part in making management decisions substantially affecting the success of the enterprise.
3. The landowner works 100 hours or more spread over a period of five weeks or more in activities connected with producing the crop.
4. The landowner does things which, considered in their total effect, show that they are significantly and materially involved in the production of farm commodities.

The following decision table may be used to determine the land eligible to be claimed for Homestead Property Tax Credit. Find the taxpayer column that applies to the particular situation, then see corresponding row under “Eligible Property” for the amount of eligible property.

Taxpayer:					
Owens farm	Y	Y	Y	Y	Y
Meets gross receipts test (see above)	Y	Y	N	N	N
Lives on farm	Y	N	Less than 10 yrs.	10 yrs. or more	N
Eligible Property:					
All farmland (doesn't have to be contiguous unless rented to others)*	X	X			
Home plus 5 acres*+			X		
Home and all contiguous or adjacent unoccupied land*				X	
None					X

* Does not qualify if the taxable value of the residential area excluding the taxable of the unoccupied farmland classified as agricultural exceeds \$135,000.

+ Renters also qualify under this category.

The definition of “homestead” for the property tax credit was amended in 1990 to exclude “unoccupied real property that is leased or rented by the owner to another person . . .” [MCL 206.508(2)]. Therefore, the renter or lessor of farmland may not claim the rent paid when computing a property tax credit.

A Farmland Preservation Tax Credit must be included in total household resources. It should be reported on the schedule of total household resources in net farm income or other taxable income. Homestead Property Tax Credits, however, are not included in total household resources. If the Property Tax Credit was included in taxable farm income, it may be subtracted in determining total household resources. Farm losses may not reduce total household resources.

Part-Year or Deceased Taxpayers, Annualization of Total Household Resources for Phase-Out

A property tax or home heating credit claim made by a part-year resident or on behalf of a deceased taxpayer (unless claimed by surviving spouse) requires annualization of total household resources to determine if his or her annualized total household resources:

1. Exceeds the threshold of \$50,000, which phases out a property tax credit, **or**
2. May require a senior citizen or a totally and permanently disabled person to use a higher percentage of total household resources to determine nonrefundable portion of property taxes. (In the final computation, only the claimant's actual total household resources are used.)

Example 1: A property tax credit is filed on behalf of a **deceased** claimant age 65 with no surviving spouse. Total household resources of \$5,230 and two exemptions are reported. Taxpayer owned a home and lived in Michigan for 155 days in 2012. Taxes levied for 2012 were \$1,865. The taxable value of the home did not exceed \$135,000.

Claimant's annualized total household resources is $366/155 \times \$5,230 = \$12,350$.

Prorated property taxes are $155/366 \times \$1,865 = \790 .

Since annualized total household resources is over \$6,000, 3.5 percent of actual total household resources must be used when computing the property tax credit.

Prorated property taxes	\$ 790
Less 3.5% of \$5,230	<u>183</u>
Property tax credit amount	\$ 607

Example 2: A **part-year** Michigan resident who lived in Michigan for 266 days received Michigan total household resources of \$30,425. Total property taxes of \$2,400 were levied on the Michigan homestead. The homestead's taxable value did not exceed \$135,000.

Claimant's annualized total household resources is $366/266 \times \$30,425 = \$41,863$. The phase-out is 10 percent after reaching \$41,001 and then 10 percent for every additional \$1,000 in total household resources. The claimant's property tax credit will be reduced by 10 percent.

Prorated property taxes ($266/366 \times \$2,400$)	\$ 1,744
Less: 3.5% of actual total household resources (\$30,425)	<u>1,065</u>
Balance	679
Multiply by 60%	407
Less: Percentage of credit subject to Phase-out provision ($10\% \times \$407$)	-41
Property tax credit	\$ 366

Separated and Divorced Claimants

Spouses who file separate Michigan income tax returns but share a household are entitled to only one property tax credit. Complete the property tax credit claim jointly, including both spouses' incomes, then divide the credit as desired. If each spouse claims a portion of the credit, attach a copy of property tax claim showing the share claimed. Two homesteads may be used for credit only if the couple is separated or divorced, each maintains a separate homestead, and each files separate federal and Michigan income tax returns. If the taxpayers file a joint federal return, they must file a joint Michigan return.

Example: Ron and Rosemary were separated March 1, 2012 and divorced December 2, 2012. Rosemary stayed in the marital home all year, and Ron rented an apartment beginning March 1, 2012. Ron paid Rosemary \$300 (half the house payment) from March through December 2012 and 40 weeks of child support at \$160 a week. Property tax bills for 2012 on the marital home were \$2,850. Ron rented his apartment for \$500 a month. Their incomes before and after separation are as follows:

Wages:	Ron	Rosemary
January 1 - February 29	\$ 7,200	\$ 5,000
March 1 - December 31	\$36,000	\$ 25,000

First calculate the property taxes that can be claimed for credit by each spouse prior to separation.

Income prior to separation:

Wife	\$ 5,000
Husband	<u>7,200</u>
Total	\$12,200

Percent of income prior to separation:

Wife	$\$5,000/\$12,200$	=	41%
Husband	$\$7,200/\$12,200$	=	59%

2012 taxes prorated for period
prior to separation

$$\$2,850 \times 2/12 = \$ 475$$

Percent claimed before separation:

Wife	$\$ 475 \times 41\%$	=	$\$ 195$
Husband	$\$ 475 \times 59\%$	=	$\$ 280$

Wife's total taxes claimed for credit
(lived in the family home for the entire year):

Before separation	$\$ 475 \times 41\%$	=	$\$ 195$
After separation	$100\% \times (\$2,850 - \$475)$	=	<u>$2,375$</u>

\$2,570

Husband's total taxes claimed for credit:

Before separation	$\$ 475 \times 59\%$	=	$\$ 280$
After separation - Rent paid	$\$ 5,000 \times 20\%$	=	<u>$\\$1,000$</u>

\$1,280

Note: Rosemary must include both the house payments made by Ron of \$3,000, as well as the child support of \$6,400 in total household resources. Ron, however, may deduct the \$3,000 alimony/separate maintenance payments in determining his total household resources. Based on the definition of household resources, he may not subtract the \$6,400 child support payments from his total household resources.

Shared Housing

When two or more single people share a home, each can file a credit claim if each is contracted to pay rent or owns a share of the home. Each should file an individual claim based on his or her own total household resources and prorated share of the taxes or rent paid. If the home is owned (not rented) and the taxable value of the shared housing exceeds \$135,000 neither person is eligible for the property tax credit. The taxable value cannot be divided between the parties.

Example 1: Adam and Andrew own a home in Grand Rapids. Both occupy the home and share the expenses for upkeep of the home. The property taxes on the home for 2012 are \$4,000. Adam and Andrew would each claim \$2,000 of property taxes on their respective property tax credits. They would each show the full taxable value of the home and write on the form “shared housing” and the percent of property taxes being claimed.

Example 2: Tim owns and occupies his home in Saginaw. He fixed up the basement and rents it for \$400 a month to Linda. Tim would be eligible to claim a property tax credit on the taxes billed on his home for 2012; however, he would have to reduce property taxes by the greater of 20 percent of the gross rent received or the amount of property tax claimed as a business expense on his federal return.

Example 3: Scott and John rent a home from Rene. The taxable value of the property exceeds \$135,000. Both names are on the contract. Monthly rental of the home was \$950; total paid during 2012 was \$11,400. All rent and expenses were split evenly between the men. Scott and John would be eligible to claim a property tax credit on one half of the rent paid. Scott and John would each be able to claim a property tax credit even though the taxable value of the home exceeds \$135,000 because the taxable value limit does not apply to renters.

Nursing Home, Home for the Aged, and Adult Foster Care Claimants

A permanent resident of a nursing home, home for the aged, or foster care home is entitled to a homestead property tax credit if the facility bills a lump sum for rent and services. The resident’s allocable share is calculated by dividing the facility’s property tax by the number of licensed beds.

If the facility receives a direct payment from a State or federal agency for the care of the resident, then the allocable share may be limited. The resident cannot claim an allocable share that is greater than the charges paid by the resident to the facility.

Example: Mrs. Redfern’s nursing home charges were billed in a lump sum of \$12,500 (for rent, food and other nursing services) to the State of Michigan. Of that sum \$12,000 was paid directly to the nursing home by the State. Mrs. Redfern paid the balance due of \$500.

Mrs. Redfern’s “allocable share” of property taxes on the nursing home, based on 100 beds and \$60,000 in real property taxes, is \$600. Since Mrs. Redfern’s total charges paid by her are less than her “allocable share,” she may use only the lesser amount of \$500 for calculating a property tax credit.

Room and Board

If the claimant pays room and board in **separate** billings, the claimant must base the credit on the rent. If the claimant pays room and board in **one** billing, the credit must be based on a prorated share of the property taxes on the facility. If the landlord does not provide this figure, divide the square footage of the claimant's living space by the total square footage of the facility, and multiply the total taxes on the facility by that percentage.

Special Housing

If the claimant resides in housing where the rent includes meals and other services (housekeeping, laundry, transportation, etc.), the credit must be based on the prorated share of the taxes on the entire property. The facility must provide the claimant with the prorated share of the property taxes for use in the credit calculation. Claimants may not calculate the credit by using the portion of the monthly payment as rent.

Service Fee Housing

If the claimant lives in housing on which service fees are paid instead of taxes, 10 percent of the rent can be claimed for credit.

Recipients of DHS Payments and Child Support Payments

MCL Section 206.520(7) allows recipients of DHS payments to reduce the amount of DHS benefits reported to them when the amounts include child support payments assigned by the Friend of the Court.

The annual statement from DHS may include child support payments made through the Friend of the Court to DHS. To determine the child support payments included in the statement, obtain a Fourth Quarter Statement from the Office of Child Support. This statement is mailed to all recipients of DHS payments. The amount reported as support is child support payments sent to DHS, and the amount reported as rebates paid is direct child support paid to the recipient.

Since the homestead property tax credit is prorated based on the percentage of income from DHS benefits, it is to the recipient's advantage to reduce the annual DHS benefits received by any child support included in this statement. The Fourth Quarter Statement from the Office of Child Support and, if available, a copy of the annual statement from DHS should be attached to the claim.

Example 1: A claimant received DHS benefits of \$12,000 in 2012, which included child support payments of \$3,000 assigned by the Friend of the Court to the DHS. If the claimant's total household resources consisted solely of DHS benefits, they would not be entitled to a homestead property tax credit. However, since one-quarter of the total DHS benefits were from child support payments assigned to DHS, they are entitled to one-quarter of the homestead property tax credit computed.

Example 2: Taxpayer receives the following for 2012:

2012 annual statement from DHS	\$8,165	
Letter from Office of Child Support or Friend of the Court:		
Support	\$7,492	
Rebates paid	600	
To compute the total household resources:		
Annual statement from DHS	\$8,165	
Rebates paid	<u>600</u>	
	8,765	
Less support paid to DHS	<u>7,492</u>	
Annual DHS benefits actually received	1,273	(FIP/DHS line)
Child support	<u>7,492</u>	(Child Support line)
Total household resources	\$8,765	

Farmland Preservation Tax Credit

Eligibility

This credit is provided for under Farmland and Open Space Preservation Act which is part of the Natural Resources and Environmental Protection Act PA 451 of 1994. This act replaced the repealed farmland preservation act known as “PA 116.” This act enables a landowner to enter into a development rights agreement (for farmland) with the State of Michigan. The agreements are designed to ensure that the land remains in agricultural use for an agreed-upon period. In return for maintaining the land in agricultural use, the landowner is entitled to certain income or property tax benefits.

The Farmland Preservation Tax Credit refunds to farmland owners the taxes in excess of 3.5 percent of their total household income on property covered by a Farmland Development Rights Agreement (FDRA) with the Michigan Department of Agriculture.

Schedule CR-5 must be completed. Use more than one Schedule CR-5 as needed. The system will not accept a substitute Schedule CR-5 in lieu of the Michigan Schedule CR-5. The entire TV for each claimed agreement must be entered on the Schedule CR-5 in the space provided. This is required even if the taxpayer is eligible to claim only a portion of the property taxes because of joint ownership(s), partnership(s), or multiple shareholders. The TV can be found on the property tax statements for each parcel.

The agreement (or contract) number is found in the lower-right corner of each agreement. The first component represents the two-digit county code where the property is located, the middle component is the actual contract number. The final component is the year of expiration (e.g., 123108 (December 31, 2008)). The actual contract number retains its original series throughout the term of the agreement. However, a letter of the alphabet may be added to indicate that the agreement was split into multiple agreements. The final six numbers change as the agreement is reduced or extended. Always use the contract number on the most recently recorded agreement. The expiration date may never be earlier than the year of the return being prepared.

Tips to Expedite Processing

- List the entire TV of an agreement regardless of the percentage of the agreement being claimed.
- Ownership indicated on property tax statements must also match ownership in farmland development rights agreement(s). If the claimed agreement does not reflect appropriate ownership, the credit may be reduced or denied.
- Multiple names on property tax statements indicate joint ownership. The taxpayer may not claim 100 percent without a signed distribution statement from all other owners. The agreement may be reduced or denied without the signed statement.
- Farmland agreement numbers consist of three components:
 - **County Code** - indicated by the first two digits of the agreement number.
 - **Contract Number** - indicated by the middle set of characters between the county code and expiration date. These characters may or may not include a letter depending on whether the agreement has been split.
 - **Expiration Date** - indicated by the last six digits of the agreement number. The first four digits are always “1231.” The last two digits are comprised of the year the agreement is to expire (e.g., “123112”). The expiration year may never be earlier than the year of the return being prepared.
- When farmland agreement numbers contain alpha characters, the alpha characters belong after the contract number but before the expiration date.
- If the expiration year entered is prior to the current tax return year, the agreement is expired and may no longer be claimed. The taxpayer must extend the agreement and provide the new expiration year before the agreement may be claimed again.

- It may be beneficial to have the taxpayer provide copies of the agreements being claimed for accuracy and to avoid processing delays.
- An MI-1040CR or MI-1040CR-7 must be filed to claim a farmland credit even if it results in a zero credit. The schedule of total household resources provided on these forms is used to verify the total household income used in computing the farmland preservation credit.
- Each agreement should only appear on one line of the Schedule CR-5. Multiple parcels for a single farmland development rights agreement must be combined to determine the entire agreement's eligible taxable value and the eligible property taxes.
- Only the portion of the tax bill used for agricultural purposes may be claimed for credit regardless of the amount of the parcel that is enrolled in the program. The qualifying portion of the parcel will be indicated on the property tax statement(s) as an agricultural or homestead percentage. Follow the instructions in the MI-1040CR-5 tax booklet under the "Property Taxes That Can Be Claimed For Credit" section to compute the eligible taxes if the bill indicates less than 100 percent exempt. Vacant farmlands classified as agricultural are not subject to the \$135,000 taxable value cap.

Computation of the Value of the Lien Imposed Upon Removal of Land From Farmland and Open Space Program

When property is removed from the Farmland and Open Space Program, the State Land Use Agency records a lien against the property. Land may be relinquished from the program for the following reasons:

1. Natural expiration of the agreement.
2. Death or permanent disability of the landowner.
3. Landowner requests relinquishment of all or a portion of an agreement.

The lien value may be computed differently based on the reason the land was relinquished. The following discussion outlines the computations required by the different ways the FDRA is relinquished.

1. Natural termination of agreement.

The value of the lien will be the amount of the farmland preservation credits attributable to the terminated agreement received by the owner in the final seven years. The final seven years shall include the year of termination. The value is computed as follows:

Step 1

Divide: The ad valorem property tax levied on property subject to the expired FDRA that was used in determining the farmland preservation credit in that year

By: The property taxes levied on property subject to all FDRAs used in determining the farmland preservation credit in that year.

Step 2

Multiply: The owner's total farmland credit on all agreements paid that year

By: The quotient in Step 1.

Step 3

Sum: The results of Step 2 may or may not be used for each of the last seven years, depending on agreement number and property taxes assessed.

2. **Landowner dies or becomes permanently and totally disabled, and a request has been granted for the release of all property covered by the FDRA.**

The value of the lien will be the total amount of the farmland preservation credit received by the owner for the payback period. The payback period and value of the lien is computed as follows:

Payback Period

Step 1

Divide: The number of years the land was enrolled in the current FDRA

By: The number of years for which the agreement was written.

Step 2

Multiply: Seven years

By: The quotient computed in Step 1.

Value of the Lien

Step 1

Divide: The ad valorem property tax levied on property subject to the FDRA being relinquished that was used in determining the farmland preservation credit

By: The property taxes levied on property subject to all FDRAs used in determining the farmland preservation credit in that year.

Step 2

Multiply: The owner's total farmland preservation credit on all agreements claimed that year

By: The quotient computed in Step 1.

3. Landowner dies or becomes permanently and totally disabled, and a request has been granted for the release of a portion of land covered by the FDRA.

The value of the lien will be the total amount of the farmland preservation credit received by the owner for the payback period. The payback period and value of the lien is computed as follows:

Payback Period

Step 1

Divide: The number of years the land was enrolled in the current FDRA

By: The number of years for which the agreement was written.

Step 2

Multiply: Seven years

By: The quotient computed in Step 1.

Allocated Credit of Entire Agreement

Step 1

Divide: The ad valorem property tax levied in that year on property subject to the FDRA that included the property to be removed.

By: The total property taxes levied on property subject to all FDRAs used in determining the farmland preservation credit in that year.

Step 2

Multiply: The owner's total farmland preservation credit in that year on all agreements

By: The quotient in Step 1.

Value of the Lien

Step 1

- Divide: The TV of the property being relinquished from the agreement
- By: The total TV of the property subject to the FDRA that included the property being removed from the agreement.

Step 2

- Multiply: The “allocated tax credit” of entire agreement
- By: The quotient computed in Step 1.

4. Landowner requests relinquishment of all or a portion of an agreement as provided by Section 36111(2)(a)(b) and 36111(a).

Termination of All Land Covered by an FDRA

Step 1

- Divide: The ad valorem property tax levied on property subject to the FDRA to be relinquished that was used in determining the farmland preservation credit in that year
- By: The property taxes levied on property subject to all FDRAs used in determining the farmland preservation credit in that year.

Step 2

- Multiply: The owner’s total farmland credit on all agreements paid that year
- By: The quotient in Step 1.

Step 3

- Sum: The results of Step 2 plus 6 percent per annum interest for each of the last seven years.

Termination of a Portion of Land Covered by an FDRA

Step 1

- Divide: The ad valorem property tax levied in that year on property subject to the FDRA that included the portion to be relinquished
- By: The total property taxes levied on property subject to all FDRAs used in determining the farmland credit in that year.

Step 2

- Multiply: The owner's total farmland preservation credit in that year on all agreements
- By: The quotient in Step 1. This is the "allocated tax credit."

Value of the Lien

Step 1

- Divide: The TV of the property being released from the agreement
- By: The total TV of the property subject to the FDRA that included the property being released from the agreement.

Step 2

- Multiply: The "allocated tax credit" for the agreement
- By: The quotient computed Step 1.

Step 3

- Sum: The results of Steps 1 and 2 plus 6 percent per annum interest for each of the last seven years.

Sale of Land

From January 1 to the day of closing, the seller (and conceivably their predecessor(s) in title) are the owner of the farmland.

For the period from January 1 to the day of closing, the seller is the person responsible for the ad valorem taxes. For income tax purposes, the IRS concludes the seller, not the buyer, pays the taxes (if the taxes are paid).

Similarly, the buyer is the owner of the farmland and is responsible for the payment of taxes (if paid) from the period of the “closing day” to December 31.

Based on the above, each owner is entitled to claim the credit for that portion of the calendar year they held title to the farmland.

Reinstatement of a Development Rights Agreement

If there is a lapse of time between the expiration and reinstatement of an agreement, the landowner is not eligible to claim a farmland preservation credit for the time the agreement had expired. The lien, which is recorded when an agreement is terminated, is discharged upon reinstatement of the development rights agreement. A subsequent lien will not be less than the lien discharged due to reinstatement.

Farmland Preservation Credit When Land Is Inherited

The taxpayer who inherited the land is not eligible for the credit until they are the owner of record and the FDRA is transferred to them by the State Land Use Agency.

Taxable Portion of Farmland Preservation Tax Credit

Taxable income for Michigan income tax purposes is defined in ITA, MCL 206.30(1), as AGI as determined in the IRC subject to certain adjustments. To the extent that a farmland preservation property tax credit is includable in an individual’s AGI, this income is taxable to this State. There is no statutory provision to exclude this income from the computation of Michigan taxable income.

Income is defined in Michigan’s ITA, MCL 206.510(1) as the sum of federal AGI, as established in the IRC, plus all income specifically excluded or exempt from the computation of the federal AGI.

Income does not include payments or credits under MCL 206.510(1). A farmland preservation tax credit is provided for in the Farmland and Open Space Preservation Act, **not the ITA**.

The part of the homestead property tax credit that applies to farm buildings and land is business related. To determine the portion that is business income, multiply the credit by the percentage that the TV of the buildings and land is to the total TV of the property (see example).

The local assessor can provide a breakdown showing how total TV was determined.

$$\begin{array}{l} \text{TV of Farmland} \\ \text{Portion of Homestead} \\ \text{and Buildings} \\ \hline \text{Total TV} \end{array} \quad \times \quad \begin{array}{l} \text{Homestead Property} \\ \text{Credit Amounts} \\ \text{Received This Year} \end{array} \quad = \quad \begin{array}{l} \text{Property Tax Credit} \\ \text{That Is Business Income} \end{array}$$

The farmland preservation tax credit amount and the business portion of the homestead property tax credit received during the year must be included in taxable income.

If, however, the MI-1040 tax refund was greater than the amount of farmland preservation credit plus the business portion of the homestead property tax credit, subtract the excess refund amount received during the year to the extent that it was included in federal AGI.

Attaching Property Tax Statement(s) When Claiming an MI-1040CR-5

For All E-Fileers: Indicate in the space provided on Schedule CR-5 if the property taxes are paid for the year of the return or for the immediately preceding year. No property tax statements are required at this time. However, keep them with the tax records, as there may be a need in the future for Treasury to request them.

For All Paper Filers: Indicate in the space provided on Schedule CR-5 if the property taxes are paid for the year of the return or for the immediately preceding year. Property tax statements for the year of the return **must** be included. These statements must include the TV, property taxes levied by millage rate, and the corresponding agreement number(s). If the tax statements do not indicate payment of property taxes and the Paid Tax Receipts box is checked on the Schedule CR-5, a copy of the previous year's property tax receipt(s) indicating payment is also required.

Note: The Paid Tax Receipt box is checked if the property taxes are either paid (for e-file) or receipts are attached. If the box is not checked, it will be assumed the property taxes are not paid nor are receipts attached. This will result in the farmland credit being issued jointly payable to the taxpayer and the appropriate county treasurer.

Farmland Taxes Eligibility Chart

The following chart describes who may claim the farmland preservation credit and what taxes are to be used in computing the farmland credit based on ownership of the land.

<u>Type of Ownership</u>	<u>Taxes Based On</u>	<u>Must Attach</u>	<u>Effective Date</u>
Partnership	1. Percent of income or ownership, or 2. Statement signed by all partners listing allowable percent for each partner	1. Federal 1065, K-1, and Schedule K, or 2. Partnership agreement, or 3. Signed statement, or 4. Completed part 2 of MI-1040CR-5	1/1/84

<u>Type of Ownership</u>	<u>Taxes Based On</u>	<u>Must Attach</u>	<u>Effective Date</u>
S Corporation*	1. Percent of stock ownership	1. Federal 1120S and Schedule K	1/1/88
*MBT filers do not qualify.			
Joint (Other Than Spouse)	1. Equal apportionment among owners, or 2. Statements signed by owners apportioning taxes the same way the revenues and expenses are divided	1. Signed statement, or 2. Completed part 2 of MI-1040CR-5	1/1/84
Life Estate or Life Lease	1. Possession, or apportionment between owner and life estate holder	1. Signed statement, or 2. Completed Part 2 of MI-1040CR-5, or 3. Copy of Life Lease Agreement	1/1/86
Grantor Trust	1. Ownership	1. Portion of trust that shows owner, or the deed	1/1/84
Trust Created by Death of Spouse	1. Ownership	1. Portion of trust that shows owner, or the deed	1/1/84
Limited Liability Company	1. Based on member's share of ownership or distributive share of ordinary income as reported by company to IRS	1. Limited liability company's federal return and schedules	1/1/96
Beneficiaries	1. Based on percentage of all other distributions from the Trust	1. Portion of Trust indicating distribution percentage, or 2. Page 2 of Federal Schedule E and K-1s of the Trust	

Repayments Under the Claim of Right Doctrine

Section 265 of the ITA allows taxpayers to claim a credit against the Michigan income tax equal to the amount of tax paid on amounts included in taxable income in a prior tax year and repaid in the current tax year.

The credit is allowed on amounts which qualify under IRC Section 1341, and are not deducted in arriving at federal AGI for the tax year.

Example: Included in Roy's 2007 AGI was \$18,000 in Supplemental Unemployment Benefits (SUB pay) from ABC, Inc. In 2012, Roy repaid the \$18,000, as it was determined he did not have the right to receive the SUB pay. The 2012 repayment qualified under IRC Section 1341 and was taken as an itemized deduction by Roy on his 2012 federal Schedule A. For the 2012 tax year, Roy is allowed a \$722 ($\$18,000 \times .0401$) credit against his Michigan income tax. Calculate the credit using the tax rate in effect for the year the amount was included in Michigan taxable income (4.01 percent), not the rate (4.33 percent) in effect for 2012, the year of the repayment. Report the credit on the line for reporting withholding taxes. Write "Claim of Right/Repayment" next to the withholding line. Attach a copy of Roy's federal Form 1040 pages 1 and 2, Schedule A, documentation of the repayment, and a calculation showing how the credit was determined on his 2012 MI-1040.

Earned Income Tax Credit

Beginning January 1, 2012, a taxpayer may claim a refundable credit against the income tax for an amount equal to 6 percent of the credit the taxpayer is allowed to claim as a credit under IRC Section 32 (i.e., the Earned Income Tax Credit (EITC)) for a tax year on a return filed under the act for the same year.

Home Heating Credit

PA 335 of 2004 amended Section 527(a) of the ITA to allow Treasury to establish a program for direct payments of energy drafts to enrolled heating providers. If a claimant's name has been submitted by the provider (Consumers Energy, DTE Energy Company, or SEMCO Energy Gas) and meets the requirements established by Treasury, the energy draft will be paid directly to the provider.

PA 169 of 2001 allows a Home Heating Credit only if there has been a federal appropriation for the federal fiscal year beginning in the tax year of federal low income home energy assistance program block grant funds of any amount. Also under PA 169 of 2001, no portion of the credit allowed shall be applied as an offset to any liability of the claimant.

The Home Heating Credit form **must be filed and postmarked no later than September 30** of the following year. The amount of the credit may be prorated depending on the amount of federal funds appropriated.

An eligible claimant for a heating credit is defined as a renter or owner of a home. In addition the claimant's income must be within the income limits listed on the eligibility charts in the MI-1040CR-7 instruction booklet. An ineligible claimant is a person who lives in a home and does not pay rent or is not an owner. The standard allowance of heating costs is prorated for eligible claimants if the home is occupied by ineligible claimants. Ineligible claimants include:

1. Full-time students claimed as dependents by another person
2. Residents of a congregate care facility (i.e., nursing home, foster care home, home for the aged, substance abuse center, etc.) who resided in the care facility for the entire year.

For individuals who rent their homestead, if at the time of filing their heating costs are included in their rent or if the heat is in someone else's name, the credit must be reduced by 50 percent.

Example: A Michigan resident whose heat is included in his or her rent claimed a 2012 home heating credit. Two federal exemptions were reported. The claimant's total household resources of \$7,475 included wages of \$3,025, DHS benefits of \$1,500, and child support of \$2,950. The claimant may claim a home heating credit of \$161.

To compute the home heating credit:

Standard allowance	\$ 584
Less THR multiplied by 3.5%	- <u>262</u>
Standard credit	322
Renters reduce credit by 50%	- <u>161</u>
Home Heating Credit	\$ 161 (subject to possible proration)

When two or more taxpayers (not related as husband and wife) share a home, each can claim a home heating credit if each has contracted to pay rent or owns a share of the house. If they share a home but are not the owners or have not contracted to pay rent, then they cannot claim a home heating credit.

To claim a credit, each eligible claimant should file a Home Heating Credit based on their total household resources and their share of the standard allowance. The standard allowance is determined from Table A in the MI-1040CR-7 instruction booklet by adding the personal exemptions of all the claimants sharing the home.

Example 1: Two women share an apartment. Each person has signed a lease and pays one-half of the rent in 2012. The standard allowance for two exemptions is \$584. Each person must use a standard allowance of \$292 ($\$584/2 = \292) to compute the credit.

If one of the individuals sharing the home is eligible for a special exemption or a dependent exemption, then she would compute her credit as follows:

The standard allowance as computed above is \$292. Then add the difference between the standard allowance for three (\$736) and the standard allowance for two (\$584) to \$292 ($\$736 - \$584 = \$152 + \$292 = \$444$). \$444 is the standard allowance for the individual with the dependent exemption.

Part-year residents or claimants filing on behalf of deceased taxpayers must prorate the standard allowance based on the number of days the taxpayer was a Michigan resident. The decedent is not eligible for the alternate credit computation.

Example 2: A 2012 Home Heating Credit* claim is filed by a **part-year** Michigan resident who resided in Michigan for 198 days. The claim is based on Michigan total household resources of \$3,500 and one exemption.

Prorated standard allowance	
($198/366 \times \$431$)	233
Less: 3.5% of actual total household resources	
(\$3,500)	<u>- 123</u>
Home Heating Credit	\$ 110 (subject to possible proration)

*No annualizing of total household resources is required when computing a Home Heating Credit.

CANCELLATION OF DEBT

If a debt owed by an individual is cancelled or forgiven, other than as a gift, the amount of the cancelled debt must be included in gross income of the individual. Therefore, any income arising from cancellation of debt (COD) included in federal AGI is subject to Michigan income tax. Forgiveness of debts owed to a seller/creditor are considered reductions to the purchase price and, generally, are not classified as cancellation of debt.

1. Q. How does a taxpayer know when a lender has forgiven a mortgage debt?
 - A. The following may be received from the lender:
 - **1099-A: Acquisition or Abandonment of Secured Property.** This is used to compute federal gain or loss if the home is transferred in a foreclosure.
 - **1099-C: Cancellation of Debt.** This reports any debt cancelled by the lender. The amount of debt cancelled is shown in box 2.
2. Q. Is COD included in federal AGI?
 - A. Generally, yes. However, there are some major exceptions (see Item 5).
3. Q. If COD is included in AGI, can it be subtracted on an MI-1040?
 - A. No.

4. Q. If COD is included in AGI must it be included in total household resources?
A. Yes.
5. Q. When, under federal law, can COD be excluded from AGI?
A. Discharge in bankruptcy, insolvency, or mortgage on a principal residence.
6. Q. When a COD is excluded from AGI, must it be added back on the MI-1040?
A. No.
7. Q. When a COD is excluded from AGI, must it be included in total household resources?
A. Usually yes, but see the exception in item 8 below.
8. Q. When can a COD on a mortgage be excluded from total household resources?
A. When the lender doesn't foreclose, but agrees to reduce the amount owed. In this case, ownership of the house does not change. This is sometimes known as a "workout." In this case, the owner would probably receive a 1099-C but not a 1099-A.
9. Q. Why isn't the COD part of total household resources in the case of a workout?
A. Because any gain or loss on the sale of the house is put off until the owner sells. The basis – a value used to compute gain or loss on a sale – is adjusted by the COD. Therefore, when the owner eventually sells the house they will recognize more gain (assuming it is sold for a gain) which will be included in total household resources at that time.
10. Q. What is a "Redemption Period?"
A. This is the phase of the foreclosure process which starts with a sheriff's sale and ends when ownership actually changes. It is usually six months.
11. Q. May the owner take a property tax credit for the time the owner lived in the home during the redemptions period?
A. Yes, even though the owner may never pay the property taxes.
12. Q. What if the (ex) owner remains in the home after the redemption period expires?
A. They may not claim property taxes for time after the redemption period expires. They may, however, take credit for any rent paid to remain living there.

RELIEF FROM TAX LIABILITY

Non-Obligated Spouse Allocation

MCL Chapter 205, Section 30a, permits spouses to apportion a joint refund as though they had filed separate returns when one spouse has a liability. A non-obligated spouse's share of the refund will not, under certain conditions, be used to offset an obligated spouse's debt.

A spouse not responsible for the liability may obtain their share of the refund by completing and filing *Income Allocation for Non-Obligated Spouse* (Form 743). Form 743 is used to determine an overpayment based on separate reporting of income, credits and exemptions.

Form 743 is issued after the processing of the income tax return and CANNOT be obtained in advance.

Form 743 must be signed by both spouses and returned within 30 days from the date Form 743 was mailed by Treasury. If it is not filed within this period, a portion or all of the joint refund will be used to offset the obligated spouse's liability. If Form 743 is returned to Treasury but is incomplete, the entire refund may be offset. Once Form 743 is filed it cannot be amended. A non-obligated spouse will **not** be permitted to commence an action to recover any amount withheld to satisfy the debt if the form is improperly filed. Form 743 should be filled out even if the taxpayer is unsure of the debt or is contesting the debt.

If the obligated spouse's signature cannot be obtained, Form 743 may still be filed but must list the reason why the obligated spouse's signature is missing.

Complete Form 743 using the figures from the original return even if you discover that the Michigan income tax return needs to be amended. Do **not** attach Form 743 to an amended return as the processing of the original refund will be delayed. The taxpayer may later file an amended return taking into consideration the refund requested on the original return.

Falsely reporting any information on Form 743 will result in a penalty of \$25 or 25 percent of the excessive amount claimed, whichever is greater.

Relief From Joint and Several Liability on Joint Returns

Innocent spouse relief, separation of liability, and equitable relief may be granted by Treasury for the portion of the tax liability that is attributable to the understatement of tax or the underpayment of tax. Treasury shall use the standards set forth in IRC Section 6015 and related federal interpretation in matters regarding relief from joint and several liability.

Individuals requesting relief shall provide information regarding spousal relief that has been granted for federal income tax liability or other documentation or information to support the individual's request.

FIDUCIARY INFORMATION

Legislative Changes to The Michigan Income Tax Act for 2012

PA 38 of 2011 and several other public acts contain extensive changes to Michigan's IIT that will affect fiduciary income tax returns filed for the 2012 tax year. The income tax rate was 4.35 percent, but a rate reduction to 4.25 percent occurred on October 1, 2012. The annualized rate for 2012 is 4.33 percent for filers who have a calendar tax year. Fiscal year filers must annualize the rate based on their tax year. Fiscal year filers may refer to the chart included in the MI-1041 instruction booklet. In addition, beginning in 2012, the following credits are no longer available:

- City Income Tax Credit
- Community Foundation Credit
- Homeless Shelter/Food Bank Credit
- Individual or Family Development Account Credit
- Public Contribution Credit
- Renewable Energy Surcharge Credit
- Vehicle Donation Credit

General Information

A copy of the U.S. 1041 must be filed with *Fiduciary Income Tax Return* (Form MI-1041), and Schedules 1, 2, and 3 must be completed, if applicable. Schedule 4 must be completed if the estate or trust is filing as a nonresident.

A MI-1041 estate return must be filed on behalf of the estate of the deceased to report any income received after the date of death. An estate return is only entitled to the federal exemption allowance of \$600.

Resident Estate or Trust

A MI-1041 must be filed if a U.S. 1041 return was filed or if there was income taxable to Michigan that was not included on the U.S. 1041 (such as interest and dividends income from obligations of states other than Michigan).

Nonresident Estate or Trust

An MI-1041 must be filed if income or gain from Michigan sources exceeds federal fiduciary exemptions. (This would include income or gain from real or tangible personal property located in Michigan; income from business, trade, profession, or occupation conducted in Michigan; income from services performed in Michigan; or income earned, received, or acquired in Michigan.)

Grantor Trust

Michigan does not require a grantor trust to file a MI-1041 when the grantor is a trustee and is treated as the owner of the trust's assets per the IRC. Instead, report the trust's income, deductions, and credits on the grantor's MI-1040. (*Ref to IRC Reg 1.671-4.*) The fiduciary, in addition to not being required to file a MI-1041, would not be required to provide copies of federal returns or federal Schedule K-1s for the grantor trust.

A grantor trust is a separate legal entity under state law but it is not recognized as a separate taxable entity for income tax purposes, because the grantor or other substantial owner has not relinquished complete dominion and control over the trust.

See IRC Sections 671 through 678 for more information on the characteristics of grantor trusts.

Allocation of Michigan Net Adjustments to Trust Beneficiaries

A beneficiary must attach Schedule K-1 or a letter from the fiduciary to their MI-1040 return. The Schedule K-1 or the letter must show the name of the trust, federal identification number, and the income and Michigan adjustments to be included on the beneficiary's MI-1040 and MI-1040D.

The allocation of Michigan net adjustments must be in proportion to the beneficiary's respective share of distributable net income of the estate or trust as defined in the IRC.

If the estate or trust has no distributable net income for the taxable year, refer to MCL 206.36(2) which states:

“The respective shares of an estate or trust and its beneficiaries, including, solely for the purpose of this allocation, nonresident beneficiaries, in the additions and subtractions to taxable income shall be in proportion to their respective shares of distributable net income of the estate or trust as defined in the internal revenue code. If the estate or trust has no distributable net income for the taxable year, the share of each beneficiary in the additions and subtractions shall be in proportion to his share of the estate or trust income for the year, under local law or the terms of the instrument, which is required to be distributed currently and any other amounts of such income distributed in the year. Any balance of the additions and subtractions shall be allocated to the estate or trust. If capital gains and losses are distributed or distributable to a beneficiary or beneficiaries under the internal revenue code, the fiduciary shall advise each beneficiary of his share of the adjustment under section 271. The election or failure to elect under section 271 with respect to capital gains and losses taxable to the estate or trust shall not affect the beneficiary's right to elect or not elect under section 271.”

There will be occasions where the additions or subtractions would be attributable to capital gains that were not distributed. The taxpayer should identify any additions or subtractions attributable to the capital gains or losses that were not distributed according to the same percentage as the distributable net income.

Taxable Income of Nonresident Beneficiary of Michigan Trust

A nonresident beneficiary's taxable income is subject to the allocation and apportionment rules of the ITA. There is no exclusion for the income passed through to a nonresident beneficiary from a Michigan trust if the income is allocable or apportionable to this State under the provisions of Chapter 3 of the ITA.

IRS MATCH

The IRS provides Treasury with information regarding taxpayers' federal tax returns in accordance with IRC Section 6103(d). Following is a summary of the IRS match programs.

The **delinquent match program** identifies taxpayers who filed their federal income tax returns from a Michigan address but did not file Michigan returns. Treasury sends these taxpayers a letter of inquiry requesting that a Michigan income tax return be filed. The letter indicates the amount of tax that is due based on the reported federal AGI and federal exemption allowances.

The **AGI match program** identifies taxpayers who reported a different amount of AGI on their federal income tax returns than on their State income tax returns. Treasury sends a letter of inquiry to the taxpayers indicating the amount of AGI reported on their federal return and the Michigan return. Tax due is computed on the difference between the federal and State return. Since total household resources is affected, the property tax credit and home heating credit (if applicable) are recomputed adding the difference to the amount due.

The **CP 2000 program** identifies taxpayers who failed to report income that was reported to the IRS by third parties. Treasury sends a letter of inquiry to the taxpayers indicating the source and the amount of the unreported income, as well as the amount of income tax and interest due on that income.

The IRS reports the results of all audits conducted on individuals who are Michigan residents. This information is then matched against amended returns filed by the taxpayers. If discrepancies exist or if amended returns are not filed, the taxpayers will receive a letter of proposed income tax adjustments and the amount due. If the IRS made a determination, taxpayers need to submit that information to the State of Michigan.

If taxpayers disagree with the information in the letter of inquiry, they should write to Treasury within the specified time. If they received a redetermination or any other documentation from the IRS, they should submit a copy of it attached to their letter.

TAXABILITY OF FEDERAL OBLIGATIONS

Income from certain U.S. Obligations, reduced by any expenses in carrying the obligation used in arriving at federal AGI, can be subtracted on the Michigan return.

The following U.S. Obligations are exempt from Michigan Individual Income Tax:

U.S. Government Bonds	U.S. Saving Bonds - Series E, F, G, and H
U.S. Government Certificates	U.S. Treasury Bills and Notes

Obligations issued by the following U.S. Agencies are exempt:

Banks for Cooperatives	Federal Intermediate Credit Banks
Central Banks for Cooperatives	Federal Intermediate Credit Corp.
Commodity Credit Corp.	Federal Land Banks
Consolidated Bonds	Federal Land Banks Association
Consolidated Discount Notes	Federal Savings and Loan Insurance Corporation
Consolidated System Bond, Series L	Home Owner's Loan Corp.
Consolidated Systemwide Discount Notes	Joint Stock Land Banks
District of Columbia	Maritime Administration
Farm Credit Banks	Production Credit Association
Farmers Home Corp.	Small Business Administration
Federal Deposit Insurance Corp.	Student Loan Marketing Association (Sallie Mae)
Federal Farm Credit Bank	Tennessee Valley Authority (bonds only)
Federal Farm Loan Corp.	U.S. Housing Authority
Federal Farm Mortgage Corp.	U.S. Maritime Commission
Federal Financing Banks	U.S. Possessions (obligations Puerto Rico, Virgin Islands, etc.)
Federal Home Loan Banks	U.S. Postal Service (bonds)
Federal Housing Administration (General Insurance Fund Debentures)	

The following debentures issued under the General Insurance Fund are exempt:

Interest from Armed Services Housing Mortgage Debentures
Interest from debentures issued under War Housing Insurance Law
Interest from debentures to acquire rental housing projects

The following General Services Administration Public Building Trust Participation Certificates are exempt:

1st series A through E
2nd series F
3rd series G
4th series H and I

The Guam Obligations issued by Government of Guam are exempt.

Notes: Income from exempt U.S. Obligations received by the taxpayer through Money Market Funds, Money Market Certificates, Mutual Funds, Trusts, etc., generally qualifies for a subtraction.

Treasury Bill Futures are not U.S. obligations.

The following U.S. Obligations are taxable:

- Building and Loan Associations
- Credit Union Share Accounts
- District of Columbia Armory Board
- Export/Import Bank of Washington, D.C.
- Federal Home Loan Mortgage Corporation (Freddie Mac) mortgages and other securities
- Federal Housing Administration (debentures, notes, and participation certificates)
- Federal National Mortgage Association (Fannie Mae) participation and other instruments
- Federal Savings and Loan Associations
- Government National Mortgage Association (Ginnie Mae) (debentures, notes, and participation certificates)
- International Bank for Reconstruction and Development (World Bank)
- Panama Canal Bonds
- Participation Certificates issued by the Federal National Mortgage Association
- Philippine Bonds
- U.S. Department of Agriculture Farmers Home Administration Insured Notes
- U.S. Government Insured Merchant Marine Bonds

Other examples of taxable interest from federal obligations:

- Debentures issued to mortgages or mortgages foreclosed under the provisions of the National Housing Act
- Farmer's Home Administration
- Federal Home Loan time deposits
- FSLIC secondary reserve prepayments
- Government National Mortgage Association participation certificates and on Federal Home Loan Mortgage Corporation participation certificates in mortgage pools
- Interest-bearing certificates issued in lieu of tax exempt securities, such income losing its identity when merged with other funds
- Participating loans in the Federal Reserve System for member banks (Federal Funds)
- Promissory notes of a federal instrumentality
- Refunds of federal income tax
- U.S. Postal Service certificates and savings deposits

INCOME ALLOCATION CHART

The following chart may be used to determine which types or sources of income are taxable to Michigan. This chart is not inclusive of all types of income, but reflects the most common.

<u>Type of Income</u>	<u>Allocate To</u>
Salaries, wages, tips, director fees, commissions, etc.	State where earned and state of residence. A Michigan resident may be entitled to a credit if income also taxed by another state. Exception: Residents of reciprocal states are not taxed by Michigan on this type of income and vice versa.
Deferred compensation:	
1. Principal portion	State of residence when received. (See RAB 1997-2 for tax years prior to 1996.)
2. Interest portion	State of residence when received.
Dividends and interest	State of residence. Exception: If earned by a partnership or S corporation, allocate or apportion to the state of the business activity if business income.
Business income or loss (Schedule C)	State where business activity takes place. Business income attributable to Michigan and one or more states must be apportioned. (Form Schedule H.)
Partnerships, S corporations, or other flow-through entities income or loss:	
1. Ordinary business income or (Schedule E)	State where business activity takes place.
2. All other business income or	State where business activity takes place.
3. Nonbusiness income or loss	State of residence.

<u>Type of Income</u>	<u>Allocate To</u>
Capital gain or loss (Schedule D or 4797):	
1. Intangible personal property such as stocks, bonds, commodities, futures, etc.	State of residence unless business income.
2. Section 1231	State where property is located unless business income.
3. Real property	State where real property is located unless business income.
Pension, retirement, annuity, qualifying IRA distributions, and Social Security benefits	State of residence when received.
Rent and royalty income or loss (Schedule E):	
1. Tangible and intangible personal property	Michigan if used in this State, or if a resident and not taxable in the state where property is used.
2. Real property (includes royalties for minerals which came from real property such as oil and coal)	State where real property is located unless business income.
Estate or trust income or loss	Look to type and source of income and apply guidelines in this chart.
Farm income or loss (Schedule F)	State where farm is located.
Unemployment compensation	State of residence.
Alimony and state and local refunds	State of residence when received.
Gambling winnings from casinos and licensed horse tracks located in Michigan, and winnings from raffle, bingo, and prizes won in Michigan	State where earned and state of residence. (Michigan lottery won by nonresidents is taxable in Michigan.)

INCOME AND DEDUCTIBLE ITEMS, SUMMARY CHART

Notes: N = Not included
Y = Included
AGI = Adjusted Gross Income
THR = Total Household Resources

<u>Income Items</u>	<u>AGI</u>	<u>Michigan Taxable Income</u>	<u>THR</u>
Alimony received	Y	Y	Y
Awards, prizes (in excess of \$300 for THR)	Y	Y	Y
Bingo:			
First \$300	Y	Y	N
In excess of \$300	Y	Y	Y
Bonuses	Y	Y	Y
Business (Schedule C) income or loss:			
In Michigan (except Michigan oil and gas subject to severance tax)	Y	Y	Y*
From another state and/or net income from Michigan oil and gas subject to severance tax	Y	N	Y*
Capital gains:			
100% taxable	Y	Y	Y
Note: Senior citizen born before 1946 may subtract interest, dividends, and capital gains included in AGI. The maximum deduction must be reduced by the pension subtraction. Allowable deduction is the smaller of the calculation or actual total interest, dividends, and capital gains.			
This subtraction is adjusted by the percentage increase in the U.S. Consumer Price Index for the preceding calendar year. See MI-1040 instruction booklet for the year being reviewed.			
Gains on sale of principal residence	N	N	Y
Casualty loss reimbursement in excess of loss of property	Y	Y	Y
Child support payments:			
Payer	Y	Y	Y
Receiver	N	N	Y

* All business income and loss must be netted before considering the effect on THR. If the netting results in a loss, this cannot be used to reduce THR. Exception: Farmland Preservation Tax Credit continues to be based on household income and not THR. Business losses and NOL deductions are allowed in household income. (See MI-1040CR-5 instructions.)

<u>Income Items</u>	<u>AGI</u>	<u>Michigan Taxable Income</u>	<u>THR</u>
Chore service payments:			
Provider of service	Y	Y	Y
Receiver of service	N	N	N
Commissions	Y	Y	Y
Compensation for personal services rendered	Y	Y	Y
Damages for personal injury or sickness	N	N	Y
Deferred compensation	Y	Y	Y
Director's fees	Y	Y	Y
Disability income (limited)	Y	Y	Y
Policeman and Fireman On-Duty "J-Days"	N	N	Y
Dividends received (see Note under "Capital gains")	Y	Y	Y
Educational expenses paid by employer	N	N	Y
Employee business expenses: cash allowance or reimbursement	Y	Y	Y
Energy assistance grants or tax credit	N	N	N
Estates or trusts income or loss	Y	Y	Y*
FIP benefits (see "Public assistance . . .")			
Farm income or loss from:			
Michigan	Y	Y	Y
Another state	Y	N	Y*
Farm portion of homestead property tax credit	Y	Y	N
Farmland preservation tax credits	Y	Y	Y
Foreign earned income exclusion	N	N	Y
Foster care payments	N	N	Y

* All business income and loss must be netted before considering the effect on THR. If the netting results in a loss, this cannot be used to reduce THR. Exception: Farmland Preservation Tax Credit continues to be based on household income and not THR. Business losses and NOL deductions are allowed in household income. (See MI-1040CR-5 instructions.)

<u>Income Items</u>	<u>AGI</u>	<u>Michigan Taxable Income</u>	<u>THR</u>
Gambling:			
Winnings (in excess of \$300 for THR)	Y	Y	Y
Losses:			
Professional gamblers (Net losses)	Y	Y	N*
All others	N	N	N
Gifts - cash:			
First \$300	N	N	N
Excess over \$300	N	N	Y
Government grant for home repair or improvement	N	N	N
Government payments made directly to educational institutions or housing projects	N	N	N
Health, life (unless benefits exceed \$50,000), and accident insurance premiums paid by employer	N	N	N
Homestead property tax credits	Y	N	N
Housing allowance for clergy	N	N	Y
Inheritance bequest or devise from:			
Non-spouse	N	N	Y
Spouse	N	N	N
Interest received on:			
Banking, savings and loan assoc., etc., accounts	Y	Y	Y
Insurance dividends	Y	Y	Y
Land contracts	Y	Y	Y
Money market and savings certificates	Y	Y	Y
Municipal bonds issued by another state	N	Y	Y
Municipal bonds issued by Michigan	N	N	Y
Tax refunds	Y	Y	Y
U.S. Obligations (only specific agencies exempt)	Y	N	Y
Interest taxable to Michigan (see Note under "Capital gains")			
Life insurance proceeds paid to:			
Non-spouse	N	N	Y
Spouse	N	N	N
Life insurance - cash in amount in excess of premiums	Y	Y	Y
Living expenses of claimant paid by another person	N	N	Y

* All business income and loss must be netted before considering the effect on THR. If the netting results in a loss, this cannot be used to reduce THR. Exception: Farmland Preservation Tax Credit continues to be based on household income and not THR. Business losses and NOL deductions are allowed in household income. (See MI-1040CR-5 instructions.)

<u>Income Items</u>	<u>AGI</u>	<u>Michigan Taxable Income</u>	<u>THR</u>
Loans received or paid	N	N	N
Long-term disability payments received (if all or part of premium paid by employer)	Y	Y	Y
Lottery:			
100% taxable (in excess of \$300 for THR)	Y	Y	Y
Installment winners of Michigan lottery who won prior to 12-30-88	Y	N	Y
Lump sum distribution included in 10-year averaging (for individuals born before 1936)	N	N	Y
Medicare payments	N	N	N
Military wages or retirements	Y	N	Y
Combat pay not excluded from taxable on federal return	Y	N	Y
Combat pay excluded from taxable on federal return	N	N	Y
Moving expenses, reimbursement:			
Moving into Michigan	Y	Y	Y
Moving out of Michigan	Y	N	N
Net operating loss deduction [the NOL is allowed in household income when computing the Farmland Preservation Tax Credit]	Y	Y	N
Partnership income or loss:			
In Michigan (except net income from Michigan oil and gas subject to severance tax)	Y	Y	Y*
From another state and/or net income from Michigan oil and gas subject to severance tax	Y	N	Y*
Pension and retirement benefits for persons born after 1945 [<i>refer to Pension and Retirement Benefits section of this manual.</i>]	Y	Y/N	Y
Private pensions (e.g., qualified annuity plans) up to amount allowed as subtraction for claimed year for persons born before 1946	Y	N**	Y
Private pensions or qualified annuity plans in excess of amount allowed as subtraction for claimed year for persons born before 1946	Y	Y	Y
Public Pensions (federal, state, or municipal governments) for persons born before 1946	Y	N	Y

* All business income and loss must be netted before considering the effect on THR. If the netting results in a loss, this cannot be used to reduce THR. Exception: Farmland Preservation Tax Credit continues to be based on household income and not THR. Business losses and NOL deductions are allowed in household income. (See MI-1040CR-5 instructions.)

** This subtraction is adjusted by the percentage increase in the U.S. Consumer Price Index for the preceding calendar year. (See the MI 1040 instruction book for the year being reviewed.)

<u>Income Items</u>	<u>AGI</u>	<u>Michigan Taxable Income</u>	<u>THR</u>
Public assistance payments from DHS			
FIP paid to grandparents for care of grandchildren	N	N	Y
FIP paid to parents for children	N	N	Y
Public health officer's income:			
Michigan resident	Y	Y	Y
Nonresident	Y	N	N
Railroad sick pay	Y	Y	Y
Railroad Tier 1 retirement benefits:			
Taxable amount for persons born before 1946	Y	N	Y
Nontaxable portion	N	N	Y
Railroad Tier 2 retirement benefits for persons born before 1946	Y	N	Y
Railroad unemployment benefits	N	N	Y
Refunds - Michigan state and local income tax	Y	N	N
Relief in kind	N	N	N
Rents and royalties income or loss:			
In Michigan (except net income from Michigan oil and gas royalties subject to severance tax)	Y	Y	Y
From another state and/or net income from Michigan oil and gas royalties subject to severance tax	Y	N	Y
Note: All rent and royalty income and loss must be netted before considering the effect on THR. If the netting results in a loss, this cannot be used to reduce THR.			
Retirement benefits (see "Private and Public pensions . . .")	Y	N/Y	Y
S corporation business activity:			
In Michigan (except net income from Michigan oil and gas subject to severance tax)	Y	Y	Y*
In another state and/or net income from Michigan oil and gas subject to severance tax	Y	N	Y*
Scholarship, stipends, education grants, GI bill benefits	N	N	Y
Note: Scholarship must be received and used for qualified tuition and related expenses such as fees, books, supplies, and equipment required for courses of instruction at a qualified organization.			

* All business income and loss must be netted before considering the effect on THR. If the netting results in a loss, this cannot be used to reduce THR. Exception: Farmland Preservation Tax Credit continues to be based on household income and not THR. Business losses and NOL deductions are allowed in household income. (See MI-1040CR-5 instructions.)

<u>Income Items</u>	<u>AGI</u>	<u>Michigan Taxable Income</u>	<u>THR</u>
Scholarships or grants received and used for nonqualified expenses that are included in federal AGI such as room and board	Y	Y	Y
Severance pay	Y	Y	Y
Sick pay	Y	Y	Y
Social Security benefits:			
Taxable amount	Y	N	Y
Nontaxable portion	N	N	Y
Stipends received for benefit of grantor (interns, resident doctors)	Y	Y	Y
Strike pay	Y	Y	Y
Supplemental gain (Form 4797)	Y	Y	Y
Supplemental unemployment benefits	Y	Y	Y
Surplus foods	N	N	N
Unemployment compensation	Y	Y	Y
Unemployment compensation from railroad	N	N	Y
Vacation allowance	Y	Y	Y
Veterans Administration benefits	N	N	Y
Wages, salaries, tips	Y	Y	Y
Workers' Compensation	N	N	Y
<u>Deductible Items</u>	<u>AGI</u>	<u>Michigan Taxable Income</u>	<u>THR</u>
Alimony paid	Y	Y	Y
Capital losses:			
Short-term, maximum \$3,000 (THR, maximum \$3,000)	Y	Y	Y
Long-term, maximum \$3,000 (THR, maximum \$3,000)	Y	Y	Y
Casualty Loss:			
Claimed as itemized deduction	N	N	N
Claimed as business deduction	Y	Y	Y

<u>Deductible Items</u>	<u>AGI</u>	<u>Michigan Taxable Income</u>	<u>THR</u>
“Claim of Right” (repayment of items previously included in income) taken as:			
Itemized deduction (taken as Michigan credit)	N	N	N
Federal tax credit (taken as Michigan credit)	N	N	N
Deduction reflected in AGI	Y	Y	Y
Health and accident insurance paid by taxpayer for self and family (not including pre-tax payroll deductions)	N	N	Y
IRA or Keogh, (payments to)	Y	Y	Y
Moving Expenses:			
Moving to Michigan	Y	Y	Y
Moving out of Michigan	Y	N	N
Penalty on early withdrawal of savings	Y	Y	Y
Self-employment tax deduction	Y	N	Y
Venture Capital deduction	Y	N	N

MICHIGAN CITIES LEVYING AN INCOME TAX

The following Michigan cities levy an income tax of **1 percent** on residents and **0.5 percent** on nonresidents except those cities where rates are indicated:

Albion	Ionia
Battle Creek	Jackson
Big Rapids	Lansing
Detroit (as of 2011, 2.45% on residents, 1.23% on nonresidents)*	Lapeer
Flint	Muskegon
Grand Rapids (1.5% on residents, 0.75% on nonresidents)	Muskegon Heights
Grayling	Pontiac
Hamtramck	Port Huron
Highland Park (2% on residents, 1% on nonresidents)	Portland
Hudson	Saginaw (1.5% on residents, 0.75% on nonresidents)
	Springfield
	Walker

*As of the date of this publication.

CORPORATE INCOME TAX (CIT)

NEW

On May 25, 2011, Public Act (PA) 38 of 2011, Michigan Corporate Income Tax (CIT) was enacted into law. The CIT took effect January 1, 2012 and replaces the Michigan Business Tax (MBT), except for certain taxpayers that wish to retain certain certificated credits. Taxpayers that have MBT credits defined under PA 36 of 2007 and PA 39 of 2011 as certificated credits may choose to continue to file under the MBT to claim those credits.

In order to make Michigan competitive and foster a climate of economic growth, the CIT was enacted to streamline the process of reporting taxes. The CIT will only apply to C corporations, entities taxed as C corporations for federal income tax purposes, and all insurance companies and financial institutions. Individuals, partnerships, S corporations, trusts, and flow-through entities are not subject to CIT. However, flow-through entities may be subject to withholding. The tax rate levied on C corporations is 6 percent of the CIT tax base after allocation or apportionment.

Insurance companies and financial institutions are taxed separately under the CIT. Insurance companies are taxed on 1.25 percent of gross direct premiums written on property or risk located or residing in Michigan. Financial institutions are subject to a tax equal to 0.29 percent of apportioned net capital. Due to the distinct treatment under CIT, insurance companies and financial institutions are addressed separately in this section.

Filing Requirements

Filing Thresholds

Taxpayer means a corporation, insurance company, financial institution, or Unitary Business Group (UBG), that is liable for a tax, interest, or penalty under this part.

Any standard taxpayer engaged in business activity in Michigan whose allocated or apportioned gross receipts are \$350,000 or more in a tax year is required to file a tax return. In general, gross receipts include any activity by the taxpayer whether in intrastate, interstate, or foreign commerce which results in a direct or indirect benefit or gain with certain exceptions. For tax years of less than 12 months, a taxpayer's gross receipts filing threshold is calculated by multiplying \$350,000 by a fraction, the numerator of which is the number of months in the taxpayer's tax year and the denominator of which is 12. In calculating the filing threshold of a C corporation, the apportioned or allocated gross receipts of a flow-through entity shall be imputed to each of its C corporation members based upon the same percentage that each member's proportionate share of distributive income is to the total distributive income of the flow-through entity. Any taxpayer with an annual liability of less than or equal to \$100 is not required to file or pay under the Act.

Special rules apply for a UBG. The filing requirement is determined on a group basis before intercompany eliminations. Therefore, if the filing threshold is met for the group, every member of the group will be included on the UBG's return regardless of the member's gross receipts.

The gross receipts filing threshold does not apply to insurance companies and financial institutions. However, these taxpayers are not required to file or pay if annual liability is less than or equal to \$100.

Tax Year

A CIT taxpayer's tax year is the calendar year, or the fiscal year ending during that calendar year. If a return is made for a fractional part of a year, tax year means the period for which the return covers. Generally, a taxpayer's tax year is for the same period covered by its federal income tax return. However, for the first return required under CIT, a fiscal year filer's tax year may differ from what is covered by its federal income tax return.

A taxpayer that has a 52 or 53 week tax year beginning not more than seven days before the end of any month is considered to have a tax year beginning on the first day of the subsequent month.

For a UBG, the unitary return will include all member tax years ending within the designated member's tax year. A person included in a UBG that joins or departs the UBG other than at the beginning or end of that person's federal tax year shall have a tax year beginning at the start of its federal tax year and ending on the date of joining or departing the unitary business group and another tax year beginning on the date immediately after joining or departing the unitary business group and ending with the conclusion of its federal tax year.

Due Dates and Extensions

Generally, an annual or final return must be filed with the Michigan Department of Treasury (Treasury) by the last day of the fourth month after the end of the taxpayer's tax year. Thus, a return for calendar year 2012 is due April 30, 2013. Fiscal year taxpayers will be granted an automatic extension for their 2012 fiscal year annual CIT return. Returns for fiscal years ending in 2012 will be due the same date as 2012 calendar year returns.

Taxpayers seeking an extension must file a *Application for Extension of Time to File Michigan Tax Return* (Form 4) by the due date of the CIT annual return. However, if the taxpayer received a federal extension and indicates that information on Form 4 and sends the necessary payment, then the taxpayer will receive an automatic extension to the last day of the eighth month following the original due date. **Keep in mind that an extension of time to file is not an extension of time to pay.** An extension of time to file will also extend the statute of limitations.

Estimated Returns and Payments

Corporate, financial institution, and insurance company taxpayers that reasonably expect to have a liability of more than \$800 for the tax year must make quarterly estimated payments and returns. Each payment must approximate the taxpayer's tax liability for the quarter or 25 percent of estimated annual liability. Second, third, and fourth quarter payments should include any necessary adjustments for overpayments or underpayments from a previous quarter. A taxpayer with a tax year of less than four months is not required to file an estimated tax return or remit estimated payments.

Note: Taxpayers that calculate and pay estimates pursuant to IRC 6655(e) may use the same methodology to make CIT estimated payments.

In order to avoid interest and penalty, the sum of all estimated payments made must be at least 85 percent of the annual liability and each quarterly payment must reasonably approximate the liability incurred in the quarter. For the 2012 tax year there will be no prior year safe harbor provision in place to avoid penalty and interest. However, for tax years after the first CIT tax year, a taxpayer may qualify for the safe harbor provision if the previous year's liability was \$20,000 or less. Under this safe harbor, a taxpayer must submit four equal estimated payments, the sum of which equals the previous tax year's liability.

When the prior CIT tax year is a period of less than 12 months, the \$20,000 threshold test will be applied to the annualized liability of the short year. To annualize the partial-year return, take the tax liability for the year, multiply by 12, then divide that result by the number of months in the tax year. The estimated payments made in four equal installments must equal the annualized prior year's tax liability. For the taxpayer's first year under CIT of less than 12 months, the amounts paid with each quarterly return shall be proportional to the number of payments made in the first tax year.

Example 1: The taxpayer's prior CIT return was for a period of six months, with a tax liability of \$5,000. To satisfy the requirements of making four equal installments based on the prior year's tax liability, the taxpayer would need to make estimated payments of \$10,000 ($(\$5,000 \times 12) / 6 = \$10,000$).

Example 2: The taxpayer's prior CIT return was for a period of six months, with a tax liability of \$15,000. This taxpayer would not be able to use the safe harbor based on the prior year's tax liability because the annualized tax liability in the prior year for this taxpayer is \$30,000. ($(\$15,000 \times 12) / 6 = \$30,000$). Therefore, to avoid penalty and interest charges, this taxpayer must make total estimated payments equal to at least 85 percent of the total liability for the tax year and the amount of each estimated payment must reasonably approximate the tax liability for the quarter.

Estimated returns and payments for calendar year taxpayers are due to Treasury on April 15, July 15, October 15, and January 15. Fiscal year taxpayers should make returns and payments on the appropriate due date which is fifteen days after the end of their fiscal quarters. If filing monthly using *Combined Return for Michigan Taxes* (Form 160) and not making remittances by electronic funds transfer, monthly payments may be filed on the 20th day of the month. However, for taxpayers required to make remittances by electronic funds transfer or otherwise not using Form 160, CIT estimates remain due on the 15th day of the month following the final month of the quarter. The estimated CIT for the quarter must always reasonably approximate the liability for the quarter.

Rather than submitting four equal installments, a taxpayer may choose to make larger payments early in its current tax year so that it has paid the sum which equals its immediately preceding tax year's tax liability before the fourth quarter. However, making larger payments late will not satisfy the safe harbor provision.

Example 1: A taxpayer has a prior year tax liability of \$10,000. The taxpayer makes a timely first quarter estimate of \$5,000 and a timely second quarter estimate of \$5,000. The taxpayer makes no estimated payments for the remainder of the year. The taxpayer will have satisfied the safe harbor based on the prior year's tax liability.

Example 2: A taxpayer has a prior year tax liability of \$10,000. The taxpayer does not make a first quarter estimate, but makes a timely second quarter estimate of \$10,000. The taxpayer makes no estimated payments for the remainder of the year. The taxpayer will not have satisfied the safe harbor based on the prior year's tax liability because there was no first quarter estimate.

Computation of First Tax Year Less Than 12 months

Taxpayers with a federal fiscal year beginning in 2011 and ending in 2012 must file two short period returns. The first short period MBT return will cover the period ending December 31, 2011. The second short period return will report the taxpayer's initial CIT liability for the period beginning January 1, 2012, through the end of the fiscal year.

If a taxpayer's CIT tax year ends before December 31, 2012, the tax may be computed by applying either the annual or actual method (see below). The choice between the annual and actual calculation methods applies only to the first year under the CIT. The calculation method chosen by the taxpayer for the first CIT short year must be the same as the method used by the taxpayer when computing the final MBT return for the other portion of the taxpayer's same tax year. The two calculation methods employed to compute the first tax year of less than 12 months are the Annual or Actual Methods.

Annual Method

The tax base may be computed as if the CIT Act was effective throughout the taxpayer's 2011-2012 federal tax period. The gross receipts will be multiplied by a fraction, the numerator which is the number of months of the federal period that fall in 2011 or 2012, and the denominator which is the number of months in a full federal period (typically 12).

Actual Method

The tax may be computed based on actual business activity occurring in the final/initial short period in accordance with the method of accounting used in prior fiscal years, which reflects the actual tax base attributable to the period.

Completing Forms

Treasury anticipates that the 2012 CIT forms and instructions will be available on the same schedule as the quarterly and annual returns for the other Michigan taxes. Quarterly estimated CIT forms were mailed to taxpayers starting in early January 2012 for payment of their CIT estimates. When the legislature adjourns for the year in December 2012, annual returns will be finalized, posted on our Web site, and sent to the printers. We anticipate that paper forms and instructions will be available for distribution to the public in January 2013.

Before beginning with the *Annual Return* (Form 4891), all appropriate federal returns should be completed.

If preparing a UBG return, complete the *Data on Unitary Business Group Members* (Form 4897) first as this form provides the data that is required on the 4891.

To complete the Annual Return, the following steps are suggested:

1. Determine whether the taxpayer has nexus with Michigan.
2. Determine whether the taxpayer has \$350,000 or more in gross receipts that are allocated or apportioned to Michigan.

If it is determined that a taxpayer must file a CIT return, then the taxpayer should determine if a UBG exists and if a Form 4897 is needed.

Insurance companies and financial institutions should review general instructions to their annual returns, *Insurance Company Annual Return For Michigan Business And Retaliatory Taxes* (Form 4905) and *Business Tax Annual Return For Financial Institutions* (Form 4908), respectively.

Amending a Return

For the CIT, Taxpayers will file a separate amended form to amend returns. To amend, select either the annual, insurance, or financial amended return form and follow the instructions on that particular form.

To amend a return to claim a refund, the taxpayer must file within four years of the due date of the original return. Interest will be paid beginning 45 days after the claim is filed or the due date of the return, whichever is later. If a taxpayer is amending a return to report a deficiency, penalty, and interest may apply from the due date of the original return.

If changes are made to the federal income tax return that affect the CIT tax bases, filing an amended return is required. If an amended return is filed within 120 days after a final determination by the IRS, penalty will be avoided.

Tax Base

CIT is levied on corporations with business activity in Michigan at a rate of 6 percent of the CIT base after allocation or apportionment. Business activity is broadly defined to include the activities of a taxpayer undertaken for gain, benefit, or advantage. The CIT base is business income with certain additions and subtractions before apportionment and a business loss deduction after apportionment. A taxpayer may use available business loss incurred under CIT after December 31, 2011. Business income is federal taxable income.

Corporation means a person that is required or has elected to file as a C corporation at the federal level. An entity that has elected to file as a corporation at the federal level will be subject to this tax along with traditional C corporations. Corporation does not include a financial institution or insurance company, as those regulated industries are taxed separately.

Flow-through entity means an S corporation, general partnership, limited partnership, trust, limited liability partnership, or a limited liability company which is not taxed as a corporation at the federal level for the tax year.

Certain entities are exempt from taxation such as entities exempt from federal income tax. A foreign person domiciled in a subnational jurisdiction of a NAFTA member country that does not impose a business tax on a similarly situated taxpayer domiciled in Michigan is also exempt from CIT. *[Reference to Michigan Compiled Law (MCL) 206.625 for more information on exemptions from the CIT.]*

Nexus

A person has nexus with Michigan if the person:

- is physically present in the State for more than one day,
- actively solicits sales in Michigan and has gross receipts of \$350,000 or more sourced to Michigan, or
- has an ownership or beneficial interest in a flow-through entity (directly or indirectly through one or more flow-through entities) which has substantial nexus in this State.

Actively solicits means:

- Speech, conduct, or activity that is purposefully directed at or intended to reach persons within this State and that explicitly or implicitly invites an order for a purchase, or
- Speech, conduct, or activity that is purposefully directed at or intended to reach persons within this State that neither explicitly nor implicitly invites an order for a purchase or sale, but is entirely ancillary to requests for an order for a purchase or sale.

Physical presence means any activity conducted by the taxpayer or someone acting in a representative capacity for the taxpayer. Physical presence does not include the activities of professionals providing services in a professional capacity if that activity is not associated with the taxpayer's ability to establish and maintain a market in this State.

Gross receipts is the entire amount received by the taxpayer, determined using the taxpayer's federal method of accounting, less certain exclusions. Gross receipts include amounts attributable to an ownership interest in a flow-through entity.

Apportionment

For a taxpayer whose business activities are confined solely to Michigan, the tax base is allocated wholly to the State. A taxpayer that has business activities subject to tax within and without the state will apportion its tax base using a 100 percent sales factor. Business activity is subject to tax outside of this State if the taxpayer is subject to a business privilege tax, a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporate stock tax, or if the other state has jurisdiction over the taxpayer, whether or not that state does subject the taxpayer to a tax.

The sales factor is a fraction, the numerator of which is total sales of the taxpayer made in Michigan during the tax year and the denominator of which is total sales everywhere made by the taxpayer during the tax year.

Sales is broadly defined to include the sale of tangible personal property, intangible property, services, and the rental, lease, licensing, or use of tangible or intangible property including interest that constitutes business activity. Sales of tangible personal property are sourced based on the ultimate destination at the point that the property comes to rest. Sales from the lease/rental of tangible personal property and income from royalties or the use of intangible property are sourced on where the property is used. Sales of services are sourced according to where the benefit of the service is received.

If a taxpayer has either directly or indirectly, an ownership or beneficial interest in a flow-through entity, the business income directly attributable to the business activity of that flow-through entity is apportioned to Michigan using the sales factor of the flow-through entity, unless the flow-through entity is unitary with the taxpayer.

For a UBG, “sales” includes sales in this State of every person included in the UBG without regard to whether the person has nexus in this State. However, sales between persons included in a UBG will be eliminated in calculating the sales factor. If a flow-through entity is unitary with the taxpayer, the group’s sales factor includes the sales of the flow-through entity. Sales must also be eliminated between the taxpayer and flow-through entities that are unitary with the taxpayer.

Special sourcing rules exist for securities brokerage services, regulated investment companies, mortgages, other loans, credit card receivables, loan servicing fees, investment, and trading activities, transportation services, telecommunications services, and private communication services.

Credits

Small Business Alternative Credit

The small business alternative credit is the only credit in CIT. The credit is available to a taxpayer, other than insurance companies and financial institutions, with gross receipts that do not exceed \$20,000,000 and with adjusted business income minus the loss adjustment that does not exceed \$1,300,000 as adjusted annually for inflation using the Detroit consumer price index. The taxpayer will also be disqualified if an officer or shareholder receives more than \$180,000 in compensation, or if compensation plus share of business income exceeds that amount (allocated income disqualifier).

The credit will be reduced by 20 percent for every \$5,000 that an officer's or a shareholder's compensation or share of business income exceeds \$160,000. The credit is also phased out by a fraction based on the amount by which the taxpayer's gross receipts exceed \$19 million.

A UBG may qualify for the credit, but a disqualifier or reduction percentage applies to the entire group if it applies to any one member of the group. The gross receipts and adjusted business income thresholds are those of the UBG and are calculated at the group level. The allocated income disqualifier is calculated for an officer or shareholder using all amounts paid or allocable to the officer or shareholder by all members of the UBG. The reduction percentages of the credit are calculated in the same manner. This credit is calculated without regard to intercompany eliminations.

Example 1: A taxpayer that is a unitary business group is disqualified from taking the credit if that unitary business group includes a member that is an LLC taxed as a corporation and any one shareholder of any one member of the LLC receives more than \$180,000 in shareholder compensation.

Example 2: The credit is reduced by 20 percent if the taxpayer is a unitary business group that includes a member that is a corporation and the compensation and directors' fees of an officer of that member corporation exceed \$160,000 but are less than \$165,000.

Credit Recapture

A taxpayer that has claimed a credit under either Single Business Tax (SBT) or MBT which had a recapture provision and fails to comply with any terms of the credit agreement must add back to its tax liability under CIT, the amount of the credit or a percentage of the amount of the credit claimed. In the case of recapture, the taxpayer's liability will increase under CIT in the year the taxpayer failed to satisfy the conditions of the credit agreement.

For a taxpayer that claimed an Investment Tax Credit under the SBT or MBT, recapture will occur under the CIT at a rate which the credit was used under either of the previous taxes. Recapture will be required when the tangible asset for which the credit was claimed is sold, transferred out-of-state or otherwise disposed of during the tax year. The recapture amount will be added back to the taxpayer's CIT liability.

A taxpayer is required to file and report recapture even if the taxpayer is below the filing thresholds (see Filing Requirements).

Certificated MBT Credits

A taxpayer that has been approved to receive, has received, or has been assigned a certificated credit under MBT before January 1, 2012, but has not fully claimed or exhausted the credit before that date, may make an election to continue paying tax under MBT and claim that credit. (See the MBT Chapter of this text for more information.)

Unitary Business Groups

A UBG is defined as “a group of United States persons that are corporations, insurance companies, or financial institutions, other than foreign operating entity, 1 of which owns or controls, directly or indirectly, more than 50% of the ownership interest with voting rights or ownership interests that confer comparable rights to voting rights of the other members, and that has business activities or operations which result in a flow of value between or among members included in the unitary business group or has business activities or operations that are integrated with, are dependent upon, or contribute to each other.”

Calculation of Liability

UBGs are treated as a single taxpayer. Unitary returns are filed by taxpayer type: either corporation or financial institution. Insurance companies do not file combined returns. Transactions between members of the group are eliminated from calculation of the tax base and apportionment factor. In general, components used to determine tax liability relate to the group as a single taxpayer, not to the individual members that comprise the group. The tax base of a unitary business group is the sum of the business income of each group member minus any income and related deductions arising from inter-group transactions. Certain additions and subtractions to business income are outlined in MCL 206.623(2) and must be made before allocation or apportionment to arrive at the unitary group's income tax base. After the tax base is allocated or apportioned, the tax base is adjusted by available business loss. The business income of each member should reflect the accounting method that member used to compute its federal taxable income.

Eliminations

Eliminations apply to transactions between any members of the UBG, not just members that report on this return. For example, if the UBG includes standard taxpayers (not owned by and unitary with a financial institution in the UBG), an insurance company, and a financial institution, transactions between a standard taxpayer member and an insurance or financial member are eliminated whenever elimination is required, despite the fact that the insurance and financial members are not reported on this return with standard taxpayer members. However, there is no elimination with an otherwise related entity if the related entity is excluded from the UBG.

Example 1: A UBG is comprised of A, B, and C. A and B are both standard taxpayers, and C is an insurance company. Even though company C files a separate tax return for insurance companies, the intercompany transactions between all three entities would be eliminated in preparing the standard tax return.

If a transaction occurs between two members of a UBG on a date that is included in the tax return for one member, the group is required to eliminate the side of the transaction that is included on this return even when the other member may not be included on that return (due to different year-ends of these members). The other side of the same transaction will be eliminated on the group return for the filing period in which the other member reports the transaction.

Example 2: A UBG is comprised of A and B. A has a calendar year-end of December 31, 2012, and B has a fiscal year-end of June 30, 2012. A is the designated member. A pays B rent in the amount of \$2,000 per month for the 2010 calendar year and \$4,000 for the 2012 calendar year. For the 2012 tax filing, Company B would eliminate from gross receipts six months' rent at \$2,000 and six months' rent at \$4,000 for a total of \$36,000.

Company B would also eliminate \$36,000 from business income. Company A would eliminate from business income 12 months of rental expense at \$4,000 for a total of \$48,000. This will cause a timing difference for intercompany eliminations that will reverse when a member ceases to exist or is no longer a part of the UBG.

Intercompany eliminations are not performed when calculating the filing threshold.

Example 3: A UBG is comprised of A, B, C, D, and E, each with \$80,000 in gross receipts. Assuming allocation of the tax base to Michigan, the gross receipts of the UBG are \$400,000. Since \$400,000 exceeds the \$350,000 filing threshold, the taxpayer is required to file a return and pay the tax. The fact that no member of the UBG would meet the filing threshold if considered individually is immaterial, therefore, A, B, C, D, and E would all be included in the UBG return.

Transactions with financial institutions and insurance company members of the group are eliminated from the corporate unitary return.

The Designated Member

Every UBG must appoint a Designated Member (DM) who will be responsible for filing the return on behalf of the group. Only the DM will be responsible for registering with the State and all CIT returns will be filed under its taxpayer identification number. Only the DM may file a valid extension request for the UBG. Treasury maintains the UBG's CIT tax data under the DMs name and account number. Each member of the UBG will be listed on the group's annual return.

If the member who owns or controls the other members of the UBG has nexus with Michigan, then that controlling member must be the DM. Otherwise, the controlling member must appoint any group member with nexus to serve as the DM. The DM must remain the same every year unless the DM ceases to be a member of the UBG or the controlling member engages in activity in Michigan that subjects that member to nexus.

Insurance Companies

Insurance companies will pay a premiums tax instead of the CIT. The premiums tax is calculated at 1.25 percent of gross direct premiums written on property or risk located in Michigan. Direct premiums do not include premiums on policies not taken, returned premiums on canceled policies, receipts from the sale of annuities, receipts on reinsurance premiums if the tax has been paid on the original premiums and direct premiums do not include the first \$190,000,000 of disability insurance premiums written in this State, other than credit insurance and disability income insurance premiums, of each insurance company subject to the tax. This exemption shall be reduced by \$2.00 for each \$1.00 by which the insurance company's gross direct premiums from insurance carrier services in this state and outside this state exceed \$280,000,000.

Insurance companies are permitted a limited number of insurance-specific credits. Under MCL 206.637(1) an insurance company may claim a credit against amounts paid to the:

- Michigan worker's compensation placement facility pursuant to Chapter 23 of the insurance code of 1956. *[Reference: PA 218, MCL 500.2301 to 500.2352]*
- Michigan basic property insurance association pursuant to Chapter 29 of the insurance code of 1956. *[Reference: PA 218, MCL 500.2901 to 500.2954]*
- Michigan automobile insurance placement facility pursuant to Chapter 33 of the insurance code of 1956. *[Reference: PA 218, MCL 500.3301 to 500.3390]*
- Property and casualty guaranty association pursuant to Chapter 79 of the insurance code of 1956. *[Reference: PA 218, MCL 500.7901 to 500.7949]*
- Michigan life and health guaranty association pursuant to Chapter 77 of the insurance code of 1956. *[Reference: PA 218, MCL 500.7701 to 500.1180]*

In addition, insurance companies are allowed a credit up to 50 percent of the examination fees paid by an insurance company during the tax year. The final credit available to insurance companies is for an insurance company subject to the worker's disability compensation act of 1969 (*reference: PA 317, MCL 418.101 to 418.941*). An insurance company may claim a credit against the tax imposed in an amount equal to the amount paid during that tax year by the insurance company pursuant to section 352 of the worker's disability compensation act of 1969 (*reference: PA 317, MCL 418.352*), as certified by the director of the bureau of worker's disability compensation. If the amount of this particular credit exceeds the tax liability of the insurance company, the excess shall be refunded, without interest, to the insurance company within 60 calendar days of receipt of a properly completed annual return.

The tax year for an insurance company is the calendar year. The due date for the annual return for an insurance company is before March 2 after the end of the tax year. An insurance company does not qualify for an automatic extension to file the annual return.

An insurance company is subject to tax under the gross direct premiums tax or the retaliatory tax, whichever is greater.

Financial Institutions

Financial Institution is generally defined as a bank holding company, national bank, state chartered bank, and state chartered savings bank, federally chartered savings association, or a federally chartered farm credit system institution. In addition, any entity that is directly or indirectly owned by any of the entities listed above and is a member of a UBG is considered a "Financial Institution". Financial institutions that have substantial nexus in the State are subject to a franchise tax. A financial institution has nexus with Michigan if:

- Physically present in the State for more than one day,

- Actively solicits sales in Michigan and has gross receipts of \$350,000 or more sourced to Michigan, or
- Ownership or beneficial interest in a flow-through entity directly, or indirectly through one or more flow-through entities, which has substantial nexus in this State.

Actively solicits is defined as speech, conduct, or activity that is purposefully directed at or intended to reach persons within this State and that explicitly or implicitly invites an order for a purchase or sale or is when speech, conduct, or activity that is purposefully directed at or intended to reach persons within this State that neither explicitly nor implicitly invites an order for a purchase or sale, but is entirely ancillary to requests for an order for a purchase or sale.

Every financial institution is taxed at the rate of 0.29 percent of its tax base after allocation or apportionment to this State. For a financial institution, tax base means the financial institution's net capital. Net capital means equity capital as computed in accordance with generally accepted accounting principles, less the average daily book value of United States obligations and Michigan obligations. In order to determine net capital, the financial institution adds net capital as of the close of the current tax year and preceding four tax years and divides the resulting sum by five. For financial institutions that have not been in existence for a period of five tax years, net capital shall be determined by adding together the financial institution's net capital for the number of tax years the financial institution has been in existence and dividing the resulting sum by the number of years the financial institution has been in existence. For a UBG of financial institutions, net capital includes the net capital of each member of the group minus the investment of one member of a group in another member of the group. Each member of a UBG must compute its net capital tax base in accordance with generally accepted accounting principles.

MICHIGAN BUSINESS TAX (MBT)

Through December 31, 2011, the Michigan Business Tax (MBT) is the only general business tax levied by the State of Michigan (State). It was enacted in Public Act (PA) 36 of 2007 to replace the previous SBT and is administered under the Revenue Act (Michigan Compiled Laws (MCL) 205.1 *et seq.*).

Beginning January 1, 2012, only those persons or UBGs that have a certificated credit, as defined at MCL 208.1107(1), may elect to be subject to the MBT in lieu of no liability (for the reason that the person is not subject to the CIT) or the CIT.

For purposes of the election, a taxpayer is either of the following:

“a person or UBG that has been approved to receive, has received, or has been assigned a certificated credit but is not subject to the tax imposed under part 2 of the Income Tax Act (ITA) of 1967, 1967 PA 281, MCL 206.601 to 206.713, and that elects under section 500 to file a return and pay the tax imposed under this act, if any, or”

“a person or UBG that has been approved to receive, has received, or has been assigned a certificated credit and that elected under section 680 of the income tax act of 1967, 1967 PA 281, MCL 206.680, to file a return and pay the tax imposed under this act, if any.”

In other words, a taxpayer or assignee holding a certificated credit, as that term is defined by the act at section 208.1107(1), may elect to remain taxable under the MBT even if it would not otherwise be subject to tax after December 31, 2011, or would otherwise be subject to Part II of the ITA.

NEW DEVELOPMENTS

Form Changes

At the time this publication went to print, the 2012 MBT booklet had not yet been finalized. Visit Treasury’s Web site at www.michigan.gov/mbt for the current status of the 2012 forms. As soon as forms are available, they may also be requested by calling (517) 636-6925.

GENERAL FILING REQUIREMENTS

Quarterly Estimates

If estimated combined MBT liability for the year is over \$800 (including surcharge, when applicable), a taxpayer making the election to remain in the MBT must file estimated returns either monthly or quarterly. Payments can be made with either of the following returns:

- *Quarterly Return* (Form 4548)
- *Combined Return For Michigan Taxes* (Form 160).

If paying quarterly, estimates are due on the 15th day of the month following the end of the taxpayer's quarter. If filing monthly using Form 160, payments are due on the 20th day of the month. For taxpayers electing to make monthly remittances by electronic funds transfer (EFT) where the requirement to file a paper Form 160 has been waived, MBT estimates remain due on the 20th day of the month following the month's end. To avoid interest charges, total estimated payments must equal at least 85 percent of the total liability for the tax year and the amount of each estimated payment must reasonably approximate the tax liability for the quarter.

For tax years 2009 and later, if the prior year's tax was \$20,000 or less, estimated tax payments may be based on the prior year's total tax liability paid in four equal payments. The taxpayer must have business activity in Michigan in the preceding year to qualify for this safe harbor. An entity not in existence or without business activity in Michigan in the preceding year would not have a "preceding year's tax liability under MBT" to qualify for the safe harbor supplied by Section 501(4)(b) and would not be able to avail itself of this statutory provision. The safe harbor is available to a taxpayer with a previous year's liability of zero as long as the taxpayer had business activity in Michigan in that prior year. The taxpayer must file a return to establish a zero liability to take advantage of the safe harbor. The safe harbor remains available to a taxpayer electing to continue under the MBT.

If the prior MBT tax year was less than 12 months (e.g., the business was opened or closed during the year), the taxpayer will need to annualize the tax to see if estimates need to be filed.

Completing Forms

Beginning January 1, 2012, the MBT is an election and is not mandatory. However, once the taxpayer files a return and claims a certificated credit, the taxpayer has made the election and must continue to file and pay under the MBT until that certificated credit and any carryforward of that credit are used up. The election is made by filing an annual MBT return or by filing *Request for Accelerated Payment* (Form 4889), to request a refund of an accelerated credit. Filing an estimate or extension will not make the election. A taxpayer must make the election in accordance with the particular certificated credit but an annual return is required regardless of the type of certificated credit claimed. Once a taxpayer elects to be subject to the MBT, it is subject to all provisions and requirements of that tax.

If a fiscal year taxpayer will not be taxable under either the CIT or MBT for its short-period tax year beginning January 1, 2012, then the taxpayer must compute the tax base for the final 2011 short-period MBT year using the accounting method that reflects the "actual" tax basis attributable to the period.

Due Dates and Extensions

Generally, annual returns are due on or before the last day of the fourth month after the end of the taxpayer's tax year. Thus, a return for calendar year 2012 is due April 30, 2013. Fiscal year taxpayers will be granted an automatic extension for their 2012 fiscal year annual MBT return. Returns for fiscal years ending in 2012 will be due the same date as 2012 calendar year returns. A taxpayer must remit any liability by the due date of the return.

A taxpayer may request an extension to file an annual return by filing *Application For Extension Of Time To File Michigan Tax Returns* (Form 4) by the due date of the annual return with payment of estimated tax. If a federal extension is filed and granted and noted on Form 4, Treasury will grant an automatic extension to the last day of the eighth month following the original due date of the return. Even if the Internal Revenue Service (IRS) has approved a federal extension, a Michigan application for extension must be filed. An extension of time to file will extend the statute of limitations. **An extension application will not be processed unless a payment is included or estimated payments have been made and are listed on the form.**

Amending a Return

A taxpayer may not amend an MBT return to revoke the election to remain in the MBT. A taxpayer may amend any return due to a change in credit amounts.

Taxpayers do not use separate forms for amending MBT returns. To amend a return, complete the appropriate form and check the box indicating an amended return in the upper-right corner of the form. To properly file an amended return, the entire return must be filed again including all attachments and schedules-not just the form or schedule that changed.

To amend a return to claim a refund, the taxpayer must file within four years of the due date or the extended due date of the original return. Interest will be paid beginning 45 days after the claim is filed or the due date of the return, whichever is later. If a taxpayer is amending a return to report a deficiency, penalty and interest may apply from the due date of the original return.

If changes are made to the federal income tax return that affect the MBT tax bases, filing an amended return is required. If an amended return is filed within 120 days after a final determination by the IRS, penalty will be avoided.

Filing Thresholds

Beginning January 1, 2012, the MBT is an election for qualifying taxpayer and is not mandatory. A taxpayer making the election to remain in the MBT is required to file an annual return. (See “Credits” listed below.)

Receipts from the production of agricultural goods by a person whose primary activity is the production of agricultural goods constitute gross receipts for MBT purposes, including the gross receipts filing threshold.

TAX LIABILITY

While subject to the MBT, a taxpayer calculates liability as the greater of:

- The taxpayer’s MBT liability after application of all credits, deductions, and exemptions and any carryforward of any unused credit as prescribed in the MBT.

- The taxpayer's liability computed under the CIT, after application of all credits, deductions, and exemptions under the CIT, as if the taxpayer were subject to the CIT, less the amount of the taxpayer's certificated credits, including any unused carryforward of a certificated credit, that the taxpayer was allowed to claim for the tax year under the MBT.

Thus, an MBT taxpayer will calculate MBT liability and hypothetical CIT liability less their certified credits determined as part of their MBT liability and pay the greater of the two.

For step one of the calculation, a taxpayer calculates the business income and modified gross receipts tax bases and applies all credits, including certificated credits, deductions, and exemptions available under the MBT. For step two, a taxpayer calculates the business income tax base under the CIT, applies all credits and deductions available under the CIT and the amount of certificated credit allowed in step one of the calculation. The amount of certificated credit allowed in step one is the amount of nonrefundable credit needed to offset MBT liability and the entire amount of a refundable credit. If the result of both steps of the calculation is a negative number, the taxpayer will receive a refund of the lower negative; but a nonrefundable credit cannot be used to reduce liability below zero. Remaining nonrefundable certificated credit may be carried forward to succeeding tax years. For a partnership or S corporation, business income includes payments and items of income and expense attributable to the business activity of the partnership or S corporation and separately reported to the members.

A taxpayer may not use a CIT business loss in the calculation of MBT liability. Similarly, once the taxpayer is no longer an eligible MBT taxpayer, it will lose any remaining business loss upon becoming a CIT taxpayer (or no longer a taxpayer).

Treasury will continue to follow the order of credits published in its forms and instructions for the MBT, 2011 tax year.

Example 1: Taxpayer Partnership calculates MBT liability of \$500 and a hypothetical CIT liability of \$750 before credit. Partnership holds a nonrefundable tool and die renaissance zone credit of \$1,000.

Step 1 of the calculation, Partnership will apply \$500 of the certificated credit amount to the \$500 liability, resulting in an MBT liability of zero

Step 2 of the calculation, Partnership will apply \$500 of credit to the CIT liability of \$750, resulting in a CIT liability after credit of \$250. Because Partnership must pay the higher of the two, its tax liability is \$250.

Example 2: Corporation calculates MBT liability of \$500 and hypothetical CIT liability of \$750 before credit. Corporation has a refundable credit of \$2,000.

Applying the credit to the MBT liability produces a liability of negative \$1,500.

Applying the same amount to the hypothetical CIT liability creates a liability of negative \$1,250.

Corporation owes the higher liability and thus receives a refund of \$1,250.

CREDITS

A taxpayer that has been approved to receive, has received, or has been assigned a certificated credit under MBT before January 1, 2012, but has not fully claimed or exhausted the credit before that date, may make an election to continue paying tax under MBT and claim that credit.

The certificated credits that qualify are:

- Anchor Company Credits
- Brownfield Redevelopment Credit
- Farmland Preservation Credit
- Film Production and Film Infrastructure Credits
- Historic Preservation Credit
- Hybrid Technology Research and Development Credit
- NASCAR Speedway and Safety Credits
- MEGA Battery Pack Credits
- MEGA Employment Tax Credit
- MEGA Federal Contract Credit
- MEGA Photovoltaic Technology Credit
- MEGA Polysilicon Energy Cost Credit
- Select Renaissance Zone Credits
 - The agricultural processing, border crossing, forest products processing, Michigan strategic fund designated and renewable energy renaissance zones for which a taxpayer has entered into a development agreement or tool and die renaissance zones for which the taxpayer has a collaborative agreement with the MSF by January 1, 2012.
- Tax vouchers for the Michigan Early Stage Venture Investment Act.

A taxpayer makes the election by filing either an annual MBT return or by filing *Request for Accelerated Payments* (Form 4889) to request a refund of an accelerated credit. Filing an estimate or extension will not make the election. A taxpayer must make the election in accordance with the particular certificated credit but an annual return is required regardless of the type of certificated credit claimed. Once a taxpayer elects to be subject to the MBT, it is subject to all provisions and requirements of that tax. Also once the taxpayer elects the MBT, it may claim all other MBT credits for which it qualifies. (See “Calculation of Liability” for more information.)

The election must be made for most certificated credits for the taxpayer's first tax year ending after December 31, 2011. However, a taxpayer with a qualifying traditional brownfield or historic preservation credit may make the election for the year in which a credit is available and is permitted to remain in the election for the life of the brownfield or historic preservation credit, but must remain in the election for the years in which credit is available. A taxpayer with a multiphase brownfield credit under MCL 208.1437(10), that makes the election, is required to continue to file and pay the MBT until the certificate is complete and the credit is used up.

A taxpayer with a qualifying brownfield or historic preservation credit that makes the election in a year in which credit is available may also elect to claim any other certificated credit for which the taxpayer is eligible in the same year, as long as eligibility for the other credit begins no earlier than the year of the claim. However, once the brownfield or historic credit is extinguished, the taxpayer may no longer remain in the MBT and loses the remainder of any other credit elected in this manner.

A taxpayer may claim a brownfield or historic preservation credit as an accelerated credit where a taxpayer is approved to receive or has received a certificated credit before January 1, 2012, and for which the certificate of completion or assignment certificate is issued for a credit for tax year beginning after December 31, 2011. The accelerated credits are claimed on a special purpose Form 4889 available on Treasury's Web site. A taxpayer may claim an accelerated credit at any point in the tax year but must also file an annual return for the tax period in which the claim is made. Accelerated credits are paid to the taxpayer within 60 days of Treasury receiving the request.

If a certificated credit is awarded to a member of a UBG, then the group and not the individual member must file any necessary returns under MBT. If the UBG makes the election the return filed by the group must include all members of the group regardless of whether a member is a corporation or a flow-through entity. The election should be made by the DM of the UBG by filing an MBT return. However, if a member of the group other than the DM files a return and makes the election, such filing will be treated as if the group made the election and all members of the group will be required to file and pay the MBT.

Assignees of Certificated Credits

Assignees holding a certificated credit may also make the election to remain in the MBT. Both the assignment and election to remain in the MBT must be completed in accordance with the requirements of a particular credit.

For example, if a taxpayer had a preapproval letter for a brownfield credit by January 1, 2012, and a certificate of completion, assignment certificate, or component completion certificate is issued for a tax year beginning after December 31, 2011, the taxpayer may assign this credit in the tax year in which the certificate of completion is issued and the assignee may make the election to remain in the MBT based on that assignment. The assignee must make the election for the tax year in which the assignment is made.

UNITARY BUSINESS GROUPS

General Filing Requirements

If a member of a UBG has a qualifying certificated credit, the group, and not the member, must make the election to file under the MBT. The election should be made by the DM of the UBG by filing an MBT return. However, if a member of the group other than the DM files a return and makes the election, such filing will be treated as if the group made the election and all members of the group will be required to file and pay the MBT. Note that the entire group is required to remain in the MBT for the time period required for the claimed certificated credit(s).

Except for a group with a brownfield or historic preservation certificated credit, the election must be made “for the taxpayer’s first tax year ending after December 31, 2011.” Because the group’s tax year is the tax year of the DM, the election must be made for DM’s first tax year ending after December 31, 2011. For taxpayers with a traditional qualifying brownfield or historic credit, the DM may make the election in the year in which a credit is available. The DM may claim an accelerated credit beginning on or after January 1, 2012.

The Designated Member

The “Designated Member” is a member of a UBG that has nexus with Michigan under MCL 208.1200 and will file the combined return required under MCL 208.1511 for the UBG. As noted, the DM makes the election to continue under the MBT on behalf of the group.

Computing Tax Liability for the UBG

All members of a UBG making the election must be included on the combined return. The flow-through entity members of the UBG will remain in the UBG and subject to the MBT if the credit election is made. The group calculates liability using all members for both steps of the comparison calculation.

Example 1: For the 2011 tax year, UBG A has three members; member one is a corporation and is the DM, member two is an S-Corporation and member three is an LLC taxed as a partnership. On December 1, 2011, member one is awarded a qualifying renaissance zone credit. In order to use that credit, member one must file an MBT return for the group’s first tax year ending after December 31, 2011. Assuming no change in ownership or control for this example, members one, two, and three must be included on that MBT return.

Example 2: UBG A has three members; member one is a corporation, member two is an S Corporation and member three is an LLC taxed as a partnership. Member one has a certificated MEGA credit of \$2,000. The group, meaning all three members, calculates its MBT liability under step one of the comparison calculation as \$900 before credits. This means the group may use \$900 of credit for an MBT liability of zero. The group calculates hypothetical CIT of \$1,000 before credits. The group offsets the liability with \$900 of certificated credit and reaches total liability \$100. The group will pay the higher liability and carry forward \$1,100 in certificated credit to the next tax year.

HELPFUL HINTS FOR FILING THE MBT RETURN

The election to remain in the MBT is made by a person or the designated member of a UBG by filing either an MBT annual return or Form 4889. Form 4889 may be filed by a taxpayer seeking to claim an accelerated refundable brownfield credit payment pursuant to MCL 208.1510. The certificate which substantiates the certificated credit must be attached to the annual return, or the accelerated credit form. Once a taxpayer files an annual return or Form 4889 claiming an accelerated credit, the taxpayer must remain in the MBT until certificated credits are extinguished.

Estimates

1. All estimated payments, extension payments, and tax returns must be filed under the UBG's designated member.
2. If making estimated payments by EFT, the associated vouchers are not required to be submitted.

**ORDER OF CREDITS
AS CLAIMED ON RETURN**

Credit	MCL	Form	Refundable	Assignable	Recapture	Carry Forward	Certification Required
NON-REFUNDABLE CREDITS							
SBT Carryforward	208.1401	4569	N	N	N	-	N
SBT Investment Tax		4569	N	N	Y	(b)	N
SBT Historic Preservation		4569	N	N	Y	(c)	N
Low-grade Hematite Pellet		4569	N	N	N	(b)	N
SBT Pharmaceutical		4569	N	N	N	(b)	N
SBT Credit Job		4569	N	N	N	(b)	N
SBT "Old" Brownfield		4569	N	N	N	(b)	N
SBT "New" Brownfield		4569	N	N	N	(c)	N
SBT MEGA Business Activity		4569	N	N	N	(b)	N
Compensation	208.1403(2)	4570	N	N	N	-	N
Investment Tax	208.1403(3)	4570	N	N	Y	-	N
Research and Development	208.1405	4570	N	N	N	-	N
Small Business Alternative	208.1417	4571	N	N	N	-	N
Gross Receipts Filing Threshold	208.1411	4571	N	N	N	-	N
Community or Education Foundation	208.1425	4572	N	N	N	-	(a)
Homeless Shelter/Food Bank	208.1427	4572	N	N	N	-	N
NASCAR Speedway Infrastructure	208.1409(1)	4573	N	N	N	-	N
Stadium	208.1410, 208.1410(a)	4573	N	N	N	-	N
Start-up Business	208.1415	4573	N	N	Y	-	Y
Public Contributions	208.1421	4572	N	N	N	-	N
Arts and Culture	208.1422	4572	N	N	N	-	N
Next Energy Business	208.1429	4573	N	N	N	-	Y
Renaissance Zone	208.1433	4595	N	N	N	-	N
Historic Preservation	208.1435	4573	N	Y	Y	10	Y
Low grade Hematite	208.1439	4573	N	N	N	5	N
Entrepreneurial	208.1441	4573	N	N	Y	-	N
New Motor Vehicle Inventory	208.1445	4573	N	N	N	-	N
Large Food Retailer	208.1447	4573	N	N	N	-	N
Mid Size Food Retailer	208.1449	4573	N	N	N	-	N
Bottle Deposit Administration	208.1451	4573	N	N	N	-	N
MEGA Federal Contract	208.1431b	4584	Y**	N	Y	10	Y
Biofuel Infrastructure	208.1460	4573	N	N	N	-	N
Bonus Depreciation	208.1461	4573	N	N	Y	10	N
Individual or Family Development Account	208.1426	4573	N	N	N	10	N
International Auto Show	208.1446	4573	N	N	N	-	N
Brownfield Redevelopment	208.1437	4584	Y**	Y	Y	10	Y
Private Equity Fund	208.1453	4573	N	N	N	-	N
Film Job Training	208.1459	4573	N	N	N	10	Y
Film Infrastructure	208.1457	4573	N	Y	Y	10	Y
MEGA Poly-Silicon Energy Cost	208.1432	4584	Y**	N	N	10	Y
MEGA Plug-In Traction Battery Manufacturing	208.1434(2)	4584	Y**	N	N	10	Y
MEGA Plug-In Traction Battery Integration	208.1434(3)	4584	Y**	N	N	10	Y
MEGA Advanced Battery Engineering Credit	208.1434(4)	4584	Y**	N	N	10	Y
MEGA Battery Manufacturing Facility	208.1434(5)	4584	Y**	N	Y	10	Y
Large Scale Battery Credit	208.1434(6)	4584	Y**	N	Y	10	Y
MEGA Anchor Company Payroll	208.1431a	4584	Y**	N	Y	10	Y
MEGA Anchor Company Taxable Value	208.1431c	4584	Y**	N	Y	5	Y
MEGA Advanced Lithium Ion Battery	208.1434(7)	4584	Y**	N	Y	10	Y
MEGA Battery Cell Sourcing	208.1434(9)	4584	Y**	N	N	10	Y
<p>* As assignee only</p> <p>** Refundable or non-refundable at the election of the taxpayer</p> <p>(a) - Community or education foundation must be certified by the Department</p> <p>(b) - May be carry forward until 2009, if the initial life span of the credit expires before 2009, the credit expires</p> <p>(c) - Initial life span of the credit</p>							

ORDER OF CREDITS
AS CLAIMED ON RETURN (cont.)

Credit	MCL	Form	Refundable	Assignable	Recapture	Carry Forward	Certification Required
REFUNDABLE CREDITS							
MEGA Research and Development	208.1407	4574	Y	N	Y	-	Y
Personal Property Tax	208.1413	4574	Y	N	N	-	N
Worker's Disability Supplemental Benefit	208.1423	4574	Y	N	N	-	Y
Next Energy Payroll	208.1429	4574	Y	N	N	-	N
MEGA Employment Tax	208.1431	4574	Y	N	Y	-	Y
Historic Preservation	208.1435	4573	N	Y	Y	10	Y
NASCAR Safety	208.1409(2)	4574	Y	N	N	-	N
Hybrid Technology Research & Development	208.1450	4574	Y	N	N	-	Y
Farmland Preservation	324.36109(2)	4594	Y	N	N	-	N
MEGA Federal Contract	208.1431b	4584	Y**	N	Y	10	Y
MEGA Photovoltaic	208.1430	4574	Y	Y	Y	-	Y
Brownfield Redevelopment	208.1437	4584	Y**	Y	Y	10	Y
Tobacco Excise Credit	208.1471	4574	Y	N	N		N
Film Production	208.1455	4574	Y	Y	N	-	Y
MEGA Poly-Silicon Energy Cost	208.1432	4584	Y**	N	N	10	Y
MEGA Plug-In Traction Battery Manufacturing	208.1434(2)	4584	Y**	N	N	10	Y
MEGA Plug-In Traction Battery Integration	208.1434(3)	4584	Y**	N	N	10	Y
MEGA Advanced Battery Engineering Credit	208.1434(4)	4584	Y**	N	N	10	Y
MEGA Battery Manufacturing Facility	208.1434(5)	4584	Y**	N	Y	10	Y
Large Scale Battery Credit	208.1434(6)	4584	Y**	N	Y	10	Y
MEGA Anchor Company Payroll	208.1431a	4584	Y**	N	Y	10	Y
MEGA Anchor Company Taxable Value	208.1431c	4584	Y**	N	Y	5	Y
MEGA Advanced Lithium Ion Battery	208.1434(7)	4584	Y**	N	Y	10	Y
MEGA Batter Cell Sourcing	208.1434(9)	4584	Y**	N	N	10	Y
<p>* As assignee only</p> <p>** Refundable or non-refundable at the election of the taxpayer</p> <p>(a) - Community or education foundation must be certified by the Department</p> <p>(b) - May be carry forward until 2009, if the initial life span of the credit expires before 2009, the credit expires</p> <p>(c) - Initial life span of the credit</p>							

UNITARY BUSINESS GROUP-CREDIT INFORMATION

Credit	MCL	Form	A	B	C	D	E
Arts and Culture	208.1422	4572	G	G	N	G	G
Biofuel Credit	208.1460	4573	E	E	N	G	G
Bonus Depreciation Credit	208.1461	4573	E	E	N	G	G
Bottle Deposit Administration	208.1451	4573	E	E	N	G	G
Brownfield Redevelopment	208.1437	4584	E	E	N	G	G
Community or Education Foundation	208.1425	4572	G	G	N	G	G
Compensation	208.1403(2)	4570	G	G	N	G	G
Entrepreneurial	208.1441	4573	E	E	N	G	G
Farmland Preservation	324.36109(2)	4594	E	E	N	G	E
Film Infrastructure	208.1457	4573	E	E	N	G	G
Film Job Training	208.1459	4573	E	E	N	G	G
Film Production	208.1455	4574	E	E	N	G	G
Gross Receipts Filing Threshold	208.1411	4571	G	G	N	G	G
Historic Preservation	208.1435	4584	E	E	N	G	G
Homeless Shelter/Food Bank	208.1427	4572	G	G	N	G	G
Hybrid Technology Research & Development	208.1450	4574	E	E	N	G	G
Individual or Family Development Credit	208.1426	4573	G	G	N	G	G
International Auto Show Credit	208.1446	4573	E	E	N	G	G
Investment Tax	208.1403(3)	4570	G	G	*	G	G
Large Food Retailer	208.1447	4573	G	G	N	G	G
Low grade Hematite	208.1439	4573	G	G	N	G	G
MEGA Anchor Company Payroll	208.1431a	4584	E	E	N	G	G
MEGA Anchor Company Taxable Value	208.1431c	4584	E	E	N	G	G
MEGA battery credits		4584	E	E	N	G	G
MEGA Employment Tax	208.1431	4574	E	E	N	G	G
MEGA Federal Contract	208.1431b	4584	E	E	N	G	G
MEGA Photovoltaic	208.1430	4574	E	E	N	G	G
MEGA Research and Development	208.1407	4574	E	E	N	G	G
Mid Size Food Retailer	208.1449	4573	G	G	N	G	G
NASCAR Safety	208.1409(2)	4574	E	E	N	G	G
NASCAR Speedway Infrastructure	208.1409(1)	4573	E	E	N	G	G
New Motor Vehicle Inventory	208.1445	4573	E	E	N	G	G
Next Energy Business	208.1429	4573	E	E	N	G	G
Next Energy Payroll	208.1429	4574	E	E	N	G	G
Personal Property Tax	208.1413	4574	G	G	N	G	G
Photovoltaic	208.1430	4574	E	E	N	G	G
Private Equity Fund	208.1453	4573	E	E	N	G	G
Public Contributions	208.1421	4572	G	G	N	G	G
Renaissance Zone	208.1433	4595	E	E	N	G	E
Research and Development	208.1405	4570	G	G	N	G	G
SBT Carryforward	208.1401	4569				G	G
SBT Investment Tax							
SBT Historic Preservation							
Low-grade Hematite Pellet							
SBT Pharmaceutical							
SBT Credit Job							
SBT "Old" Brownfield							
SBT " New" Brownfield							
SBT MEGA Business Activity							
Small Business Alternative	208.1417	4571	G	G	N	G	G
Stadium	208.1410, 208.1410(a)	4573	E	E	N	G	G
Start-up Business	208.1415	4573	E	E	N	G	G
Worker's Disability Supplemental Benefit	208.1423	4574	G	G	N	G	G

* - assets transferred between members of a UBG are not a capital investment in qualifying assets for purposes of the ITC and intercompany eliminations are irrelevant to the calculation of the ITC.

A - The test or criteria to qualify for the credit should be applied on a group basis (G) or a separate entity basis (E)

B - If the qualification test is satisfied, the calculation of the credit amount should be on a group basis (G) or a separate entity basis (E).

C - Calculation of the credit should be done after elimination of intercompany transactions (Y or N).

D - Credit should be applied against the tax liability of the group (G) or the entity (E).

E - The credit form is completed on a group basis (G) or a separate entity basis (E).

MBT AND CIT ELECTRONIC FILING

General Information

Treasury and the IRS continue to work together to provide tax preparers with an efficient method of filing their clients' business tax returns electronically.

Michigan has an enforced e-file mandate for MBT and CIT. Software developers producing MBT and CIT tax preparation software and computer-generated forms must support e-file for all eligible Michigan forms that are included in their software package. All eligible MBT and CIT returns prepared using tax preparation software or computer-generated forms must be e-filed.

Treasury will be enforcing the e-file mandate for MBT and CIT. The enforcement includes not processing computer-generated paper returns that are eligible to be e-filed. A notice will be mailed to the taxpayer, indicating that the taxpayer's return was not filed in the proper form, and content, and must be e-filed. Payment received with a paper return will be processed and credited to the taxpayer's account even when the return is not processed.

To participate in the MBT and CIT Fed/State e-file programs, e-filers must use software that has successfully completed the Michigan and IRS testing process. Confirm that the software chosen was approved for Michigan and that the Michigan e-file program is operational before transmitting returns. A list of approved software companies is available on Treasury's Web site at www.MIfastfile.org.

An organization or individual interested in participating as a software developer is required to file test returns with Michigan. Tax preparers are **not** required to file test returns with Michigan.

If, after acceptance, a tax preparer, transmitter, or software company has production problems, Treasury reserves the right to disapprove that tax preparer, transmitter, or software company for part or all of the remainder of the filing season.

To avoid posting of duplicate returns, a taxpayer filing electronically should not mail copies of federal and Michigan returns and schedules to Treasury unless requested.

When the following forms are included in a filing, the return can be e-filed but the forms listed below must be mailed.

MBT Forms:

- Form 4
- *Historic Preservation Credit Assignment* (Form 3614)
- *Film Credit Assignment* (Form 4589).

CIT Forms:

- Form 4

If tax is due on an e-file return, payments may be mailed along with *MBT E-File Annual Return Payment Voucher (MBT-V)* (Form 4576) or *CIT e-file Annual Return Payment Voucher (CIT-V)* (Form 4901) by the due date. Taxpayers may also make their payments by EFT. Application forms for EFT Debit and EFT Credit are available on Treasury's Web site at www.michigan.gov/biztaxpayments.

Treasury recognizes that there are conditions which make a return ineligible for e-file. When the computer-generated business tax return meets one or more of the Treasury-recognized e-file exceptions, the taxpayer may have to complete and attach *E-file Exceptions for Business Taxes* (Form 4833), to the front of their return or the paper filing will not be processed. Form 4833 will be generated by the software.

Attach Form 4833 to a computer-generated paper return that meets one or more of the Treasury-recognized e-file mandate exceptions. Treasury-recognized exceptions at the time of this printing include, but are not limited to:

- MBT taxpayer is filing one or more of the following forms:
 - *Qualified Affordable Housing Seller's Deduction* (Form 4579)
 - *Tribal Agreement Ownership Schedule* (Form 4597)
 - *Tribal Agreement Apportionment* (Form 4598)
- Return was prepared by a preparer who has been suspended or denied acceptance to participate in the IRS e-file program or does not have an Electronic Filing Identification Number (EFIN).
- Return was rejected by Michigan or IRS and there is no way to correct and resubmit the return electronically and software does not support State Standalone.
- Taxpayer federal return contains a form that is not eligible for e-file and the software does not support State Standalone e-file.

The following are also Treasury-recognized exceptions. However, do not attach Form 4833 to a paper return that meets one or more of the following conditions:

- The taxpayer has an organization type of individual or fiduciary
- The taxpayer does not have a Federal Employer Identification Number (FEIN)
- The return is completed by hand (with pen or pencil)
- The return is completed using forms from Treasury's Web site or Michigan tax instruction books.

The following Michigan forms and schedules may be e-filed using the MBT Fed/State e-file program for tax year 2012.

MBT Forms and Schedules

- *Historic Preservation Tax Credit* (Form 3581)
- *Annual Return* (Form 4567)
- *Nonrefundable Credits Summary* (Form 4568)
- *SBT Credit Carryforwards* (Form 4569)
- *Single Business Tax (SBT) Credit Carryforwards* (Form 4569)
- *Credits for Compensation, Investment and Research and Development* (Form 4570)
- *Common Credits for Small Businesses* (Form 4571)
- *Charitable Contribution Credits* (Form 4572)
- *Miscellaneous Nonrefundable Credits* (Form 4573)
- *Refundable Credits* (Form 4574)
- *Loss Adjustment Worksheet for the Small Business Alternative Credit* (Form 4575)
- *Schedule of Shareholders and Officers* (Form 4577)
- *Schedule of Partners* (Form 4578)
- *Unitary Business Group Combined Filing Schedule for Standard Members* (Form 4580)
- *Penalty and Interest Computation for Underpaid Estimated Tax* (Form 4582)
- *Election of Refund or Carryforward of Credits, and Calculation of Historic Preservation and Brownfield Redevelopment Carryforward* (Form 4584)
- *Investment Tax Credit Recapture From Sale of Assets Acquired Under Single Business Tax* (Form 4585)
- *Schedule of Business Activity Protected Under Public Law 86-272* (Form 4586)
- *Schedule of Recapture of Certain Business Tax Credits and Deductions* (Form 4587)
- *Insurance Company Annual Return for Michigan Business and Retaliatory Taxes* (Form 4588)
- *Annual Return for Financial Institutions* (Form 4590)
- *Farmland Preservation Tax Credit* (Form 4594)
- *Renaissance Zone Credit Schedule* (Form 4595)
- *Miscellaneous Credits for Insurance Companies* (Form 4596)
- *Unitary Business Group Combined Filing Schedule For Financial Institutions* (Form 4752)
- *Schedule of Corporate Income Tax Liability for a MBT Filer* (Form 4946)
- *Schedule of Certificated Credits* (Form 4947)
- *Schedule of Flow-Through Withholding* (Form 4966)
- *Schedule of CIT Liability for an MBT Insurance Filer* (Form 4974)
- *Schedule of CIT Liability for an MBT Financial Filer* (Form 4975)

The following Michigan forms and schedules may be e-filed using the CIT Fed/State e-file program for tax year 2012.

CIT Forms and Schedules

- *Annual Return* (Form 4891)
- *Amended Return* (Form 4892)
- *Small Business Alternative Credit* (Form 4893)
- *Schedule of Shareholders and Officers (For all Corporations Claiming the Small Business Alternative Credit)* (Form 4894)
- *Loss Adjustment for the Small Business Alternative Credit* (Form 4895)
- *Unitary Business Group Affiliates Excluded From the Return of Standard Taxpayers* (Form 4896)
- *Data on Unitary Business Group Members* (Form 4897)
- *Non-Unitary Relationships With Flow-Through Entities* (Form 4898)
- *Penalty and Interest Computation of Underpaid Estimated Tax* (Form 4899)
- *Unitary Relationships With Flow-Through Entities* (Form 4900)
- *Schedule of Recapture of Certain Business Tax Credits* (Form 4902)
- *Withholding Opt-Out Schedule* (Form 4903)
- *Insurance Company Annual Return for Corporate Income and Retaliatory Taxes* (Form 4905)
- *Insurance Company Amended Return for Corporate Income and Retaliatory Taxes* (Form 4906)
- *Annual Return for Financial Institutions* (Form 4908)
- *Amended Return for Financial Institutions* (Form 4909)
- *Unitary Business Group Combined Filing Schedule for Financial Institutions* (Form 4910)
- *Schedule of Flow-Through Withholding* (Form 4911)

Michigan will continue to accept certain binary Portable Document Format (PDF) attachments with the e-filed returns for tax year 2012 (as supported by software). A listing of the attachments will be posted to the Treasury Web site at www.MIfastfile.org.

Information from the following federal forms or schedules should be included when filing the MBT or CIT annual return.

MBT and CIT

Corporations. U.S. 1120 (pages 1 through 4) or U.S. 1120-A (pages 1 and 2), Schedule D, forms 851, 4562, and 4797. If filing as part of a consolidated federal return, attach a pro forma or consolidated schedule.

UBGs. See Form 4580 for MBT and Form 4897 for CIT. More information on federal return attachments.

Do not send copies of K-1s. Treasury will request them if necessary.

MBT

S Corporations. U.S. 1120S (pages 1 through 4), Schedule D, forms 851, 4562, 4797, and 8825.

Partnerships - U.S. 1065 (pages 1 through 5), Schedule D, Form 4797, and Form 8825.

Individuals. U.S. 1040 (pages 1 and 2), Schedules C, C-EZ, D, E, and Form 4797 (only when a member of a UBG).

Fiduciaries. U.S. 1041 (pages 1 through 4), Schedule D, and Form 4797 (only when a member of a UBG).

LLCs. Attach appropriate schedules shown above based on federal return filed.

MBT and CIT Fed/State E-file Program

Tax preparers and transmitters accepted in the IRS e-file program may participate in the MBT and CIT Fed/State e-file programs and e-file these returns through the IRS MeF program. (See www.irs.gov for more information.) A list of software developers supporting MBT and CIT e-file is available on Treasury's Web site at www.MIfastfile.org.

Michigan accepts two kinds of submissions:

1. Fed/State (linked)
2. State Standalone (unlinked).

How Fed/State (Linked) E-file Works

A State submission can be linked to the IRS submission by including the Submission ID of the federal return with the State return filing. If the State submission is linked to an IRS submission (also referred to as a Fed/State return), the IRS will check to see if there is an accepted IRS submission under the Submission ID. If there is not an accepted federal return for that tax type, the IRS will deny the State submission and an acknowledgment will be sent to the transmitter. The State has no knowledge that the State return was denied (rejected) by the IRS. If there is an accepted federal return under that Submission ID, MeF will perform minimal validation on the State submission. The validation includes verifying that the State is a participating State in the Fed/State Program. MeF will then pass along to the State what the Electronic Return Originator (ERO)/taxpayer sends in the State submission.

Note: If a state submission is linked to an IRS submission, the IRS recommends sending the IRS submission first, and after it has been accepted, sending in the state submission.

How State Standalone (Unlinked) E-file Works

If the ERO does not link the State return to a previously accepted federal return (also referred to as State Standalone return), MeF will perform minimal validation as stated above (that will include verifying that the State allows State Standalone returns), and then pass along the entire State submission that was sent in by the ERO/taxpayer.

Note: The State return is made up of a State and federal portion. The taxpayer provides both components based on what is required by the State. The IRS passes to the State just the information that has been provided by the taxpayer.

The workflow for State returns is as follows:

1. Transmitter sends State returns to IRS.
2. IRS validates the State return.
 - A. If linked return, validates IRS submission and State Participation.
 - B. If unlinked, validates State Participation.
3. If valid, IRS makes the State return available to the State.
4. The State retrieves State return from IRS.
5. The State sends receipt for State return to IRS.
6. The State will process the State return and send State acknowledgment to IRS.
7. Transmitter will retrieve the State acknowledgment from IRS.
8. The State will retrieve the Acknowledgment Notification (acknowledging Transmitter retrieved the State acknowledgment).

Application Process

To participate, applicants must first apply to the IRS and be accepted. Individuals must register with IRS e-Services and create a new (or revised) IRS application. Individuals can contact e-Help toll-free at 1-866-255-0654 for assistance with the IRS e-file Application or if unable to register for e-Services.

The definitions used by the IRS for the various categories of e-filers, EROs, transmitters, or software developers also apply for Michigan e-filing purposes.

Upon acceptance, the IRS Service Center assigns an EFIN and, if applicable, an Electronic Transmitter Identification Number (ETIN) to the applicant.

After receiving the federal acceptance information, applicants are automatically accepted into the MBT and CIT MeF programs.

IRS regulations require paid tax preparers to use Preparer Tax Identification Numbers (PTINs) for all tax returns and refund claims filed after December 31, 2010. Visit the IRS Web site at www.irs.gov for more information.

Acceptance Process

Treasury may conduct a suitability check on applicants who have been accepted in the MBT and CIT Fed/State e-file programs. Participation in the program may be denied if a company is not registered to conduct business in Michigan or if there is an outstanding tax liability with Michigan.

Treasury will use the EFIN assigned by the IRS in the MBT and CIT Fed/State e-file programs. Michigan does not assign any additional identification numbers for the MBT and CIT Fed/State e-file programs.

Signature Process for Fed/State (Linked) Returns

Michigan will accept the federal signature (8453-C, 8453-S, 8453-P, or Personal Identification Number [PIN]). The State return may be transmitted with the federal return or at a separate time. As long as there is an IRS Submission ID included with the State submission the two returns are linked together, and it is considered a Fed/State filing. Michigan does not require any additional signature documentation.

Signature Process for State Standalone (Unlinked) Returns

State Standalone returns must be signed by entering a taxpayer PIN and completing *E-file Authorization for Business Taxes* (Form MI-8879). The taxpayer may authorize the tax preparer to enter the PIN on their behalf. The MI-8879 should be retained by the tax preparer and/or taxpayer, and included in the printed copy of the return that is provided to the taxpayer.

For More Information

Visit the federal and Michigan Web sites at www.irs.gov and www.MIfastfile.org for more information on the Fed/State e-file programs.

FLOW-THROUGH WITHHOLDING (FTW)

WHAT'S NEW

On January 1, 2012, several changes to the Income Tax Act of 1967 (ITA) went into effect establishing a new withholding requirement for flow-through entities that have members, partners, or shareholders that are corporations or other flow-through entities. These changes are in addition to the amendments to the ITA made in 2003 that imposed a withholding requirement on flow-through entities that have members, partners, or shareholders that are nonresident individuals. These withholding requirements require a flow-through entity to withhold on the distributive share of business income of the member, partner, or shareholder in the same general manner used to require employers to report and remit withholding taxes on employee wages. Collectively, these withholding requirements are known as Flow-Through Withholding (FTW).

The requirement under the ITA to withhold on nonresident individuals that are members, partners, and shareholders of a flow-through entity has also changed. Business income is now apportioned using only the sales factor. In addition, fiscal year flow-through entities will file quarterly and annual withholding returns based on fiscal quarters and the fiscal year of the flow-through entity. Also effective January 1, 2012, flow-through entities previously registered and paying FTW using a Michigan Entity (ME) number must begin using their federal employer identification number (FEIN) and the new quarterly *Flow-Through Withholding Quarterly Return* (Form 4917), to report and make quarterly FTW payments. Lastly, *Statement of Michigan Income Tax Withheld for Nonresidents from Flow-Through Entities* (Form 4119), has been discontinued and is no longer available for use by the flow-through entity.

For purposes of FTW, the following definitions apply:

- **Corporation:** means an entity that is required to or has elected to file as a C corporation for federal income tax purposes.
- **Flow-through entity:** means an entity that for the tax year is treated as an S corporation, a general partnership, a limited partnership, a limited liability partnership, or a limited liability company that is not taxed as a C corporation for the tax year. Flow-through entity does not include any entity that is a disregarded entity for federal income tax purposes and does not include trusts.
- **Member:** means a shareholder of an S corporation; a partner in a general partnership, a limited partnership, or a limited liability partnership; or a member of a limited liability company.
- **Nonresident:** means an individual who is not a resident of or domiciled in Michigan.

Forms

- *Quarterly Return* (Form 4917)
- *Annual Flow-Through Withholding Reconciliation Return* (Form 4918)
- *Schedule of Unitary Apportionment for Flow-Through Withholding* (Form 4919)
- *Flow-Through Withholding Opt-Out Schedule* (Form 4920)

Withholding Requirements

There are three different withholding requirements under FTW:

Withholding on nonresident individual members. Every flow-through entity with business activity in Michigan must withhold on every member that is a nonresident individual. This withholding is done at the Individual Income Tax (IIT) rate on the distributive share of business income reasonably expected to accrue, after allocation or apportionment, to the nonresident. If the flow-through entity's year ends in 2012, the IIT rate is 4.33 percent. For tax years ending in 2013, the IIT rate is 4.25 percent. Flow-through withholding for nonresident individual members is required regardless of the entity's level of business income. Also, Flow-through withholding is not required on income protected by federal Public Law 86-272.

Withholding on corporate members. A flow-through entity with business activity in Michigan that reasonably expects to accrue more than \$200,000 in apportioned or allocated business income for the tax year must withhold on the distributive share of each member that is a corporation at the Corporate Income Tax (CIT) rate of six percent.

Withholding on intermediate-tier flow-through entity members. A flow-through entity (source flow-through entity) with business activity in Michigan that reasonably expects to accrue more than \$200,000 in apportioned or allocated business income for the tax year must also withhold on the distributive share of each member that is a flow-through entity (intermediate flow-through entity) at the CIT rate of six percent. However, the source flow-through entity may withhold at the IIT rate instead of the CIT rate if it is able to identify the ultimate member of the intermediate-tier flow-through entity as a nonresident individual and include the individual's identifying information with the annual Form 4918. Finally, the source flow-through entity is not required to withhold if it is able to identify the ultimate member of the intermediate flow-through entity as a resident individual. The IIT rate for a flow-through entity with a tax year that ends in 2012 is 4.33 percent. If its tax year ends in 2013, the IIT rate is 4.25 percent.

An intermediate-tier flow-through entity member that has no business income sourced to Michigan other than business income received from a source flow-through entity will not have to pay additional withholding and will be credited with any FTW payments made on its behalf by the source flow-through entity. This flow-through entity will, however, be required to file Form 4918 to distribute the FTW payments received from the source flow-through entity to its members.

Filing and Payment Requirements

A flow-through entity that is required to withhold on its members must file Form 4917 and pay the withholding due on a quarterly basis. A flow-through entity that is required to withhold must also file, in addition to the four quarterly returns, an Annual Reconciliation Form 4918. A flow-through entity that is an intermediate-tier member of a source flow-through entity must also file an Annual Reconciliation to distribute the amounts that have been withheld on its behalf unless the source flow-through entity has already distributed the withholding by disclosing the ultimate taxpayers on its own Annual Reconciliation. A flow-through entity that remits FTW or files an Annual Reconciliation must be registered with Michigan Department of Treasury (Treasury) for FTW in order for those payments to be properly applied and for its returns to be properly processed.

Quarterly Payments

FTW quarterly payments are reported and paid to Treasury using Form 4917. These quarterly returns and quarterly payments are due to Treasury on April 15, July 15, and October 15 of the flow-through entity's tax year and January 15 of the following year. If the flow-through entity is not a calendar year taxpayer then the flow-through entity will substitute the appropriate due dates in the flow-through entity's fiscal year that correspond to the due dates of a calendar year flow-through entity. A quarterly return is not required to be filed if the flow-through entity does not have an amount due.

Annual Reconciliation Form

A flow-through entity that is required to withhold must also file Form 4918. This Annual Reconciliation is due to Treasury no later than February 28 for calendar year flow-through entities or the last day of the second month following the end of a fiscal year flow-through entity's federal tax year.

Reporting Withholding to Members

Each flow-through entity must report several things to the members it has withheld on to allow each member to accurately file its CIT return or IIT return.

Prior to the 2012 tax year, this reporting was done using Form 4119. However, beginning with the 2012 tax year, Form 4119 is no longer available to be used. Instead, the flow-through entity may use any method to report the necessary information to its members. Treasury recommends that the flow-through entity provide this information to its members as a supplemental attachment to the member's federal Schedule K-1. Any method will be acceptable so long as the following information is conveyed to the member:

1. FEIN of the flow-through entity
2. Tax year of the flow-through entity
3. FTW paid on behalf of that member
4. Member's tentative distributive share of the flow-through entity's business income
5. Flow-through entity's sales that have been sourced to Michigan
6. Flow-through entity's total sales.

If the flow-through entity is filing a *Composite Individual Income Tax Return* (Form 807) on behalf of its nonresident individual members, then it must report to the nonresident individuals that have participated in the composite filing the:

1. FEIN of the flow-through entity
2. Tax year of the flow-through entity
3. Tax paid by the flow-through entity on behalf of the member
4. Member's tentative distributive share of the flow-through entity's business income
5. Flow-through entity's sales that have been sourced in Michigan
6. Flow-through entity's total sales.

Note: The flow-through entity may have different amounts of sales to report to its corporate and other flow-through entity members than it will for its individual members. See the explanation of apportionment for the different types of members below.

Flow-Through Withholding for Members That Are Corporations or Other Flow-Through Entities

Business Income

Business income for purposes of withholding on a member that is a corporation or an intermediate-tier flow-through entity will be governed by the same rules as those contained in the CIT. However, because FTW is concerned with the business income of flow-through entities and not corporations, business income for flow-through entities is further defined to include payments and items of income and expense that are attributable to business activity of the flow-through entity and separately reported to its members. The distributive share of business income of a flow-through entity is subject to FTW even if it is not actually distributed or paid to the member.

Income protected by Public Law 86-272 is not subject to FTW and should not be included in the flow-through entity's distributable amount of business income.

Business Income Threshold

To be required to withhold on members that are corporations or other flow-through entities the flow-through entity must first reasonably expect to have more than \$200,000 of business income in the tax year after allocation and apportionment. For purposes of calculating this threshold, the flow-through entity will apportion its business income using its sales factor—it will not use a unitary sales factor as described below.

Apportionment

A flow-through entity is only required to withhold on a member's distributive share of business income after allocation and apportionment. To apportion its business income for a member that is a corporation and for an intermediate-tier flow-through entity, the source flow-through entity will use the apportionment rules included in the CIT. The CIT includes two apportionment rules that are relevant for FTW.

The general rule provides that a flow-through entity that has members that are corporations or intermediate-tier flow-through entities will apportion the business income distributed to those members using its own sales factor. The flow-through entity's sales factor is a fraction. The numerator is the flow-through entity's sales that have been sourced to Michigan and the denominator is the flow-through entity's sales everywhere. When determining which sales are to be included in its sales factor, the flow-through entity will use the sales sourcing provisions included within the CIT. It is important to note that when apportioning its income for members that are corporations or intermediate-tier flow-through entities, the withholding flow-through entity's sales factor does not include throwback sales.

However, if the source flow-through entity is able to ascertain that the ultimate members of an intermediate-tier flow-through entity are nonresident individuals then the source flow-through entity may withhold directly on the distributive share of those ultimate members. To be able to do this, the flow-through entity must also know the name and social security number of these nonresident individuals. This information will be needed when the flow-through entity files its Form 4918. To calculate the distributive share of business income of the ultimate members and apportion that amount, the flow-through entity will use the provisions included in the IIT, as explained below.

A different apportionment rule applies if the flow-through entity is unitary with a CIT taxpayer. If the flow-through entity is unitary with a CIT taxpayer then the numerator of the sales factor used by the flow-through entity when calculating the amount of FTW due for that CIT taxpayer must include the Michigan sales of the unitary CIT taxpayer and a proportionate share of the total sales in Michigan of the flow-through entity. The denominator of this sales factor must include the total sales of the unitary CIT taxpayer everywhere and a proportionate share of the total sales everywhere of the flow-through entity.

The flow-through entity will be unitary with a CIT taxpayer if:

- The CIT taxpayer owns or controls, directly or indirectly, more than 50 percent of the ownership interest of the flow-through entity with voting rights or ownership interests that confer comparable rights to voting rights.
- The CIT taxpayer and flow-through entity have business activities or operations which result in a flow of value between the CIT taxpayer and the flow-through entity, or between the flow-through entity and another flow-through entity unitary with the taxpayer, or has business activities or operations that are integrated with, are dependent upon, or contribute to each other.

Ultimately, the apportionment percentage used by the flow-through entity to apportion the distributive share of business income received by its corporate member will be the same apportionment percentage that will be used by that corporation when computing its CIT liability. This also means that if the flow-through entity is owned by two corporations, one of which is unitary with the withholding flow-through entity, the flow-through entity must use separate apportionment percentages for each of these corporations.

Flow-Through Withholding for Members That Are Nonresident Individuals

Business Income

Income flowing through to a member of a flow-through entity is business income and is subject to the allocation and apportionment provisions of the IIT as discussed below. This income is referred to as the member's distributive share of business income. The distributive share of business income of a flow-through entity is subject to FTW even if it is not actually distributed or paid to the member.

Portfolio income is business income and is subject to allocation or apportionment. Portfolio income includes interest income, dividend income, royalty income, and net short-term and long-term capital gain (loss) from federal Schedule D Capital Gains and Losses. Resident or nonresident individual taxpayers having portfolio income from a flow-through entity with business activity in multiple states must allocate or apportion this income in the same manner as all other business income.

Income protected by Public Law 86-272 is not subject to IIT and is not subject to FTW.

Apportionment

The flow-through entity's distributive share of business income shall be allocated or apportioned to the state where the business activity takes place using a single-factor sales apportionment formula. The flow-through entity's sales factor is a fraction. The numerator is the flow-through entity's sales that have been sourced to Michigan and the denominator is the flow-through entity's sales everywhere. When determining which sales are to be included in the sales factor for nonresident individual members, the flow-through entity will use the sales sourcing provisions within the IIT. Income that is not allocated or apportioned to Michigan is not subject to FTW.

It should be noted that the computation of the sales factor is not the same for IIT as it is for the Michigan Business Tax (MBT) or the CIT. Most notably, IIT requires throwback sales to be included in the sales factor. When computing the sales factor, throwback sales for IIT follow Public Law (PL) 86-272 standards. Also, foreign sales can be in the numerator for IIT purposes. The IIT standard for determining if the taxpayer is taxable in another state uses the PL 86-272 nexus criteria. In general, a taxpayer's business must have property in another state or activity that goes beyond solicitation of sales to be taxable in the other state. The MBT and the CIT do not require throwback sales be included in either the numerator or denominator of the taxpayer's sales factor.

Composite Tax Return for Nonresident Individual Members

A flow-through entity may file a composite return, Form 807, for its nonresident individual members. If the members have no other income subject to Michigan's IIT, the composite return will satisfy the members' IIT filing requirement. To file a composite return, the flow-through entity must have two or more nonresident individual members participating in the composite return.

The participants can be other flow-through entities as well as nonresident individuals. Corporate members, however, are not able to participate in a composite return. In addition, an individual participant who has other Michigan income must also file an *Individual Income Tax Return* (Form MI-1040). When filing the MI-1040 return the nonresident individual may not subtract the income reported on the composite return but may claim a credit for their share of the tax paid on the composite return. A nonresident individual that has participated in a composite return is not able to claim as a credit the FTW payments made on its behalf.

Exemptions From Flow-Through Withholding

Flow-Through Entities That Are Exempt

Publicly Traded Partnerships and disregarded entities are not required to withhold on their members under FTW. For purposes of FTW, “publicly traded partnerships” means that term as defined under Section 7704 of the Internal Revenue Code. This exemption from the requirements of FTW applies to publicly traded partnerships that are treated as corporations as well as those that are treated as partnerships under IRC 7704(c). An entity is disregarded for purposes of FTW if it is a disregarded entity for federal income tax purposes.

Nonresident Individual Exemptions

A flow-through entity is not required to withhold on a nonresident individual member if:

1. The income available for distribution consists entirely of income exempt from IIT
2. The aggregated income available for distribution of all nonresident individual members is less than \$1,000 for that quarter.

MBT Election Exemption

A flow-through entity is not required to withhold on a member that elects to file and pay the MBT.

Opt Out Exemption

Corporate members of a flow-through entity are also able to exempt the flow-through entity from the FTW requirements by filing an exemption certificate with the flow-through entity and Treasury. If an exemption certificate is received by the flow-through entity then it is entirely exempt from the FTW requirements pertaining to that corporate member for the entire tax year. This is true no matter when the flow-through entity receives the exemption certificate, so long as the flow-through entity receives the exemption certificate within the tax year.

To qualify for this exemption, the corporation must:

- Complete the exemption certificate in the form and manner prescribed by Treasury.
- Provide a copy of the exemption certificate to the flow-through entity.

- Certify that it will:
 - File the returns required under the CIT
 - Pay the tax due under the CIT on the distributive share of the business income received from any flow-through entity in which the corporation is a member
 - Submit to the taxing jurisdiction of Michigan for purposes of collecting the tax due under the CIT and the associated penalty and interest with respect to the distributive share of the business income of that corporation.

The opt out exemption also requires the C corporation and the flow-through entity to retain a copy of the exemption certificate. The opt out exemption goes on to explain that Treasury maintains the right to revoke an exemption certificate if it finds that the C corporation or flow-through entity is not abiding by the terms of the certificate or the exemption requirements as explained above. If an exemption certificate is revoked, Treasury will notify the flow-through entity that it must begin to withhold on the C corporation's distributive share of business income under FTW within 60 days of that notice.

Revenue Administrative Bulletins (RAB)

RAB 2004-1

Composite Income Tax Return Filing

RAB 2004-01 describes the procedures for filing composite IIT returns by flow-through entities with business activity in Michigan and nonresident members in light of the enactment of legislation establishing composite filing provisions in the ITA.

RAB 2010-7

Flow-Through Entity Withholding Tax

RAB 2010-7 describes the income tax withholding of flow-through entities with respect to its members that are nonresident individuals. In addition, it explains the terms “flow-through entities,” “income available for distribution,” and “tiered entities,” and clarifies the withholding requirements of flow-through entities electing to file composite income tax returns on behalf of nonresident members. This bulletin also explains specific exemptions from the FTW requirements with respect to nonresident individual members.

Note: Due to changes to FTW beginning in 2012, the reporting requirements as described in RAB 2010-7 are no longer correct. Also, calendar reporting is no longer required for fiscal year flow-through entities and the flow-through entity's business income is now apportioned using only the sales factor. For more information and guidance for FTW, see Treasury's Web site at www.michigan.gov/taxes.

RAB 2010-8**Flow-Through Entity Withholding Tax Issues on Composite Returns**

RAB 2010-8 describes how withholding tax payments are reported and credited on composite returns by fiscal year filers and in tiered entity structures. In addition, this bulletin describes registration requirements for flow-through entities subject to flow-through entity withholding taxes.

Note: Due to changes to FTW beginning in 2012, the registration requirements and withholding and crediting of FTW on composite returns by fiscal filers as described in RAB 2010-8 are no longer correct. For more information and guidance for FTW, see Treasury's Web site at www.michigan.gov/taxes.

SALES, USE, AND WITHHOLDING TAXES

SALES TAX

The General Sales Tax Act was enacted as Public Act (PA) 167 in 1933. The tax is imposed on the seller for the privilege of making a “sale at retail” in Michigan. The tax rate has increased over the years to its current 6 percent level. Tax increases are currently restricted to authorization by amendment to the Michigan Constitution by a vote of the people.

Consumption of electricity, natural or artificial gas, and home heating fuel for residential use are taxed at a rate of 4 percent.

All sales of tangible personal property at retail in Michigan are subject to the tax unless a specific exemption applies and is claimed by the purchaser.

USE TAX

The Use Tax Act was enacted as PA 94 in 1937. Shortly after the sales tax was enacted, it became apparent that sales tax revenue was being lost by purchases of tangible personal property being made in neighboring states for consumption in Michigan. This was also recognized as a competitive disadvantage for Michigan sellers.

This tax was enacted as a tax for the privilege of storing, using, or consuming tangible personal property in Michigan. The impact of this tax is felt most by remote sellers such as mail order sellers, Internet sellers, and other similar direct marketers. To a limited extent, the use tax statute also supplements the sales tax statute by taxing some transactions that the sales tax does not reach.

“Use” is defined to include a transaction in which possession is given. This includes leases of tangible personal property as being subject to use tax. A lessor has the option of paying sales or use tax on the full cost of tangible personal property acquired for lease or paying use tax on the total lease/rental receipts. However, the lessor must first be registered to have the option available.

Certain services are also taxed “in the same manner as tangible personal property” under PA 94. These services are: intrastate telecommunications and similar communications, interstate telecommunications that either originate or terminate in Michigan when billed to a Michigan address, accommodations (hotel, motel, bed and breakfasts, vacation home, cottage rental, etc.) of less than 30 continuous days, and the laundering or cleaning of textiles under a rental agreement with a term of at least five days.

The rate has increased along with the sales tax rate over the years until reaching its current rate of 6 percent. As with the sales tax, the use tax rate is also restricted to authorization by amendment to the Michigan Constitution by a vote of the people.

The Michigan Individual Income tax return has a separate line for individuals to report and pay their use tax liability on mail order and Internet purchases made from out-of state sellers, as well as purchases while traveling in foreign countries.

EXEMPTIONS

In general, sales and use tax exemptions are based on: (1) what the item is, (2) who purchases the item, and (3) how the item is used. Frequently, a qualifying exemption from the tax will be based on a combination of these three basic exemption types.

There are currently over 100 distinct exemptions provided in the sales and use tax statutes. Generally, exemptions in one law are mirrored in the other, but there are instances when an exemption is not provided for in both laws.

ADMINISTRATIVE

Filing of Returns

When a person registers their business with Michigan to obtain a sales tax license, a use tax registration, or register as an employer for withholding, he or she is assigned a filing status, either monthly, quarterly, or annually. If their business was assigned a Federal Employer Identification Number (FEIN), they may register for business taxes online at www.michigan.gov/business. If they are unable to register online, they may complete the *Registration for Michigan Taxes* (Form 518) available at www.michigan.gov/business/taxes. It is imperative for the taxpayer to file returns based on the frequency assigned. Failure to file a return when due will result in a letter of inquiry being issued. Additional action including the issuance of an estimated tax due Intent to Assess and Final Assessment (Bill for Taxes Due) may result.

If an account is assigned a monthly or quarterly filing status, Michigan will provide *Combined Return for Michigan Taxes* (Form 160) for the liable periods. These returns will be pre-identified with the account's information and are mailed once a successful registration is completed. These pre-identified returns contain magnetic ink that facilitates processing of the return. To ensure correct application of returns and payments to an account, use only the pre-identified returns provided to the business. Form 160 and any associated payments must be received by the due date provided. Form 160 must be submitted even if no tax is due.

Payments received after the due date are subject to statutory penalty and interest.

Michigan also provides an *Annual Return For Sales, Use And Withholding Taxes* (Form 165) pre-identified with account information and filing year. All sales, use, and income tax withholding filers must submit Form 165 by the due date, even if no tax is due. Businesses identified to collect some tax at the 4 percent rate will be mailed instructions, monthly/quarterly worksheets, and an annual return providing both the 4 percent and 6 percent tax rate columns.

Not having a pre-identified return does not relieve the obligation to pay timely. If a pre-identified return is not received, complete and print Form 160 or 165 from Treasury's Web site at www.michigan.gov/taxes.

Amending Returns

Use Form 165 for prior year amendments. Form 160 is used to amend periods in the current year. If the amendment results in a credit within the current year, carry the credit forward to the worksheet for the period and reduce the tax due reported on Form 160.

Annual returns may not be amended when the withholding on a corrected *Wage and Tax Statement* (W-2) is for less than on the original W-2. These corrections must be handled between the employer and the employee or by the employee on Individual Income Tax Return (Form MI-1040). Refund requests submitted on an amended Form 165 for a W-2 adjustment will not be honored.

Additional information for amending returns is provided in the forms and instruction booklet for *Sales, Use and Withholding Taxes* (Form 78) available at www.michigan.gov/taxes.

Electronic Funds Transfer (EFT)

Payment of sales, use, and withholding taxes can be made by EFT and eliminate the need to file a monthly or quarterly paper return. Payments made by EFT must be made monthly. The only return required is Form 165, due February 28 of the following year. The *Electronic Funds Transfer (EFT) Debit Application* (Form 2248) and *Electronic Funds Transfer (EFT) Credit Application* (Form 2328) are available on Treasury's Web site at www.michigan.gov/biztaxpayments.

Due to changes in National Automated Clearing House Association (NACHA) rules, Automated Clearing House (ACH) Debit transactions are ineligible for EFT if the financial institution account used for the electronic debit is funded or otherwise associated with a foreign financial institution account to the extent that the payment transaction would qualify as an International ACH Transaction (IAT) under NACHA rules. Taxpayers should contact their financial institutions for questions about the status of their bank account. Contact Treasury's Electronic Funds Transfer Unit at (517) 636-6925 for alternate payment methods.

STREAMLINED SALES AND USE TAX AGREEMENT

Representatives from 43 states, local governments, and the business community worked for several years to implement the Streamlined Sales and Use Tax Agreement (Agreement). The Agreement is a multi-state pact providing for a system that simplifies sales and use tax collection and administration by retailers and states. Among other things, the Agreement addresses and provides for state-level administration of sales and use taxes, uniform definitions, rate simplification, uniform determination of where sales occur (sourcing), simplified exemption administration, and uniform audit and registration.

The approval of the Agreement by the Streamlined delegates did not modify the laws of any state. The determination as to whether and how to implement the terms of the Agreement rests with each state. Since approval of the Agreement, over 25 states have introduced or enacted legislation intended to conform to the provisions of the Agreement.

Michigan law does not allow for local jurisdictions, such as cities or counties, to impose sales or use taxes. Further, administration of sales and use tax is centralized at the state level in the Michigan Department of Treasury (Treasury). Accordingly, Michigan law prior to Streamlined was already in compliance with the Agreement provisions addressing those two major simplification issues. Prior Michigan law diverged from the Agreement in some of its definitions and administrative provisions. These issues included product definitions such as food and medical goods, administrative definitions such as what was included in “sales price,” and administrative provisions such as the time for filing returns. Michigan enacted legislation in 2004 to bring Michigan law into compliance with the requirements of the Agreement.

Under its terms, the Agreement would become binding and effective when at least ten states comprising at least 20 percent of the total population of states with a sales tax approved the Agreement. That threshold was achieved on July 1, 2005 with an affirmative vote on 18 states that had petitioned to become members of the Agreement.

Full members (states whose sales tax laws and policies are in substantial compliance with each of the provisions of the Agreement) include Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Oklahoma, Rhode Island, South Dakota, Vermont, Washington, West Virginia, Wisconsin, and Wyoming. Associate member states are Ohio, Tennessee, and Utah. Associate member states will become full members when certain amendments to their sales tax laws that have been approved by their legislatures become effective or following the passage of certain amendments to their conforming legislation.

The Agreement became effective on October 1, 2005. The effective date of the Agreement triggered a Web-based centralized point of sales tax registration for the member states, an amnesty period for qualified sellers, and the process for certification of software and service providers that will assist in sales tax collection responsibilities. The simplified system reduces the number of sales tax rates, brings uniformity to definitions of items in the sales tax base, reduces the paperwork burden on retailers, and incorporates new technology to modernize many administrative procedures.

The Agreement is administered by the Streamlined Sales Tax Governing Board, Inc. (Governing Board). The Governing Board has certified six service providers (CSPs) and three automated systems (CASs). The Governing Board’s contracts with CSPs provide for compensation of the CSPs by the states for taxes remitted on behalf of “volunteer” sellers. Michigan now has two methods to electronically receive Simplified Electronic Returns (SERs) and/or payment information. Automated systems (CSPs, CASs, or proprietary systems) can upload an XML file that includes the SER and/or payment information. Other sellers who don’t utilize an automated system can complete and submit an online fillable form that includes the SER and/or payment information. While current law does not require e-commerce and direct mail companies to collect and remit sales taxes on transactions that occur in states where they do not have a physical presence, it is expected that some of these companies will come forward and volunteer to collect taxes under the simplified system.

New legislation, known as the Main Street Fairness Act, was introduced in Congress in July 2010 and if passed, will require all sellers (except those qualifying for a small business exception) to collect and remit sales and use taxes with respect to remote sales sourced to member states under the Agreement.

Information on the Streamlined Sales and Use Tax Agreement and the new simplified system can be found at www.streamlinedsalestax.org.

LEGISLATION

PA 61 in 2009 amends the State Convention Development Act and changes the definition of a convention facility to include a facility leased or owned by a metropolitan authority created under the Regional Convention Facility Authority Act. The act also appropriates \$9.4 million to a metropolitan authority created under the Regional Convention Facility Authority Act for the purpose of transferring, managing, and operating a qualified convention facility.

PA 138 in 2009 amended the Streamlined Sales and Use Tax Administration Act (PA 174 of 2004) to provide a process for addressing incorrect classifications of items or transactions subject to taxation.

Under PA 138, if a seller registers to participate in the streamlined sales and use tax system, the seller may use a CSP to perform all of the seller's sales and use tax collection functions (other than its obligation to remit sales or use tax on its own purchases). A registered seller also may use a certified automated system to perform a portion of its sales and use tax collection functions, but the seller remains responsible for remitting taxes.

Under PA 138, if Treasury determined that an item or transaction was incorrectly classified as to its taxability by a CSP or by a seller using a certified automated system, Treasury would have to notify that CSP or seller of the incorrect classification. The CSP or seller would have to revise the classification within ten days after receiving the notice. If the classification was not changed within that time frame, the CSP or seller would be liable for failure to collect the correct amount of sales or use tax due to the State.

PA 156 in 2009 amends the State Convention Development Act by amending section 10 (Michigan Compiled Law (MCL) 207.630), as amended by PA 61 of 2009. This act provides for fiscal year ending September 30, 2009, that \$6.6 million shall be distributed to the general fund of this State from the Convention Facility Development Fund.

PA 37 in 2010 amends PA 94 of 1937 by amending section 21 (MCL 205.111), as amended by PA 34 of 1994. This act amends the Use Tax Act to require Treasury to deposit \$9.5 million of use tax collections into the Michigan Promotion Fund for fiscal year 2009-10 only.

PA 115 in 2010 amends the Use Tax Act to provide exemption for additional equipment used within a plant site or between plant sites operated by the same person. The additional qualifying equipment includes front end loaders, forklifts, pettibone lifts, skidsters, multipurpose loaders, knuckle-boom log loaders, tractors, and log loaders used to unload logs from trucks at a saw mill site for the purpose of processing at the site and to load lumber onto trucks at a saw mill site for purposes of transportation from the site.

PA 116 in 2010 amends the General Sales Tax Act to provide exemption for additional equipment used within a plant site or between plant sites operated by the same person. The additional qualifying equipment includes front end loaders, forklifts, pettibone lifts, skidsters, multipurpose loaders, knuckle-boom log loaders, tractors, and log loaders used to unload logs from trucks at a saw mill site for the purpose of processing at the site and to load lumber onto trucks at a saw mill site for purposes of transportation from the site.

KEY COURT CASES

Escanaba Paper Company
Michigan Court of Appeals
No. 286144
Unpublished November 19, 2009

This case involves the question as to whether a paper mill was entitled to a tax exemption as an “industrial processor” relative to “industrial processing” under the Michigan Use Tax Act arising out of the consumption and use of personal property needed to dispose of liquid and solid waste by way of a wastewater treatment facility and landfill. The plaintiff engages in the production of coated paper products. The production of coated paper products is an industrial process that creates industrial waste in both liquid and solid forms. The plaintiff disposes of its liquid waste through a wastewater treatment facility and disposes of its solid waste by burying it in a landfill. The wastewater treatment facility, the landfill, and the coated paper production facility are located on the same site. The plaintiff is required by federal and State environmental laws to properly treat and dispose of the solid and liquid waste generated. The wastewater treatment facility and the landfill enable the plaintiff to comply with these environmental laws. The plaintiff incurred expenses and used and consumed equipment in operating treatment and facility and landfill for the time period starting January 1, 1997, and running through March 31, 1999. Upon audit, the plaintiff was assessed use tax on the items that were used or consumed in connection with operating the wastewater treatment facility and the landfill for the years at issue. These items were primarily chemicals, electrical usage, and repair materials. In audits prior to the years at issue, the plaintiff was not assessed use tax on those items. The plaintiff argued it was entitled to an “industrial processing” exemption from use taxes for the years in issue.

The appeal involves use taxes to be paid on items that were used or consumed by the plaintiff in connection with the operation of its wastewater treatment facility and the landfill.

The court determined that the plaintiff is entitled to an “industrial processing” exemption on the materials used in connection with the disposal of waste in liquid and solid form.

GMAC LLC
Nuvel Credit Company LLC
Michigan Court of Appeals
No. 289261, 289262, 289263, and 289266
For Publication December 3, 2009

In this tax dispute, plaintiffs contend that a refund should be awarded pursuant to the bad debt deduction, MCL 205.541, as interpreted by the Court of Appeals in *DaimlerChrysler Services North America LLC v Department of Treasury*, despite the recent amendment to the statute clarifying the availability of the deduction. The Court held that the legislative amendment was clear and unambiguous and, therefore, plaintiffs were not entitled to the deduction.

The taxpayers filed Leave to Appeal with the Michigan Supreme Court; however, in June 2010 the court denied their leave request.

Granger Land Development Company and
Granger Waste Management Company
Michigan Court of Appeals
No. 286355
For Publication December 29, 2009

In this suit for a tax refund, defendant Treasury appeals as of right the Court of Claims order compelling Treasury to refund the full amount of taxes paid by plaintiffs Granger Land Development Company and Granger Waste Management Company (collectively Granger). On appeal, the primary question is whether the personal property at issue was exempt from Michigan's use tax.

Granger alleged, in part, that the materials and equipment that it used or consumed were used or consumed as part of an industrial process; namely, the processing of solid waste to generate gas. Because it used or consumed the materials and equipment as part of an industrial process, Granger argued that it was entitled to the exemption from sales and use taxation applicable to materials and equipment used in industrial processing.

In response, Treasury argued that the materials and equipment were not used in an industrial process or, in the alternative, that they were nevertheless not entitled to the exemption because the materials were incorporated into real property and the equipment was used to groom real property.

The court determined that because Granger uses the heavy equipment at issue to physically transport and process the waste and to erect landfill cells, the heavy machinery is being used as part of the industrial processing of the waste and not to design, engineer, construct, or maintain real property. Therefore, the Court of Claims did not err when it determined that the personal property at issue was not subject to Michigan's use tax. Accordingly, the Court of Claims did not err when it ordered Treasury to refund the use taxes paid by Granger.

Ford Motor Credit Company
Michigan Court of Appeals
No. 289781
Unpublished January 12, 2010

Same issue regarding the enabling section of MCL 205.54i was raised in GMAC LLC and Nuvel Credit Company LLC, Court of Appeals Nos. 289261 through 289263 and 289266.

Daimler Chrysler Services of North America, LLC
a/k/a Daimler Chrysler Services of North America, LLC
Michigan Court of Appeals
No. 288347
Unpublished January 21, 2010

This case was previously heard by the Court of Appeals and it was determined that the taxpayer was entitled to a bad debt deduction on vehicles that it had financed and in which the borrower later defaulted. At issue in this appeal is whether the trial court erred by determining that MCL 205.54i (a) permits a deduction for sales tax paid on property that is repossessed.

The court concluded that the Court of Claims erred to the extent that it included transactions involving repossessed property in the calculation of the bad debt deduction. The bad debt statute in effect at the time the refund claims were filed clearly states that for purposes of the bad debt deduction, a bad debt does not include repossessed property.

The taxpayer filed a Leave to Appeal this decision to the Michigan Supreme Court. On July 26, 2010, the Supreme Court issued an order refusing to hear an appeal.

REVENUE ADMINISTRATIVE BULLETINS

The following Revenue Administrative Bulletins (RABs) were issued since the last edition of this text and can be found on Treasury's Web site at www.michigan.gov/treasury. From Treasury's Web page, click on Reference Library and Revenue Administrative Bulletin.

RAB 2009-6 Exemption for Foreign Diplomatic Personnel

This bulletin explains the exemption for foreign diplomatic personnel as it relates to Michigan sales tax, use tax, airport parking tax, and convention facility development tax, and reflects the changes to the appearance of personal and mission tax exemption cards issued by the U.S. Department of State.

RAB 2009-8 Sales Tax- Food for Human Consumption

This bulletin further explains the sales and use tax treatment of food and prepared food. This new bulletin supersedes the existing bulletin RAB 2002-20.

RAB 2012-2 Notice of Change in Prepaid Gasoline Sales Tax Base

This bulletin announces the change in the prepaid gasoline sales tax rate effective June 1, 2012. Effective on that date, the prepaid rate increased to 20.5 cents per gallon.

INTERNAL POLICY DIRECTIVES

2010-1 Sales and Use Tax – Taxability of Equipment Purchased and Affixed to “Rolling Stock” After Purchase of the “Rolling Stock”

Sections 4r and 4k of the General Sales Tax Act and Use Tax Act, respectively, provide exemption for the sale of rolling stock purchased by an interstate motor carrier or for rental or lease to an interstate motor carrier and used in interstate commerce. “Rolling stock” is defined as a qualified truck, a trailer designed to be drawn behind a qualified truck, and parts affixed to either a qualified truck or a trailer designed to be drawn behind a qualified truck.

The issue is whether equipment purchased and affixed to qualifying trucks or trailers that do not replace an item that was a component of the truck or trailer qualify for exemption. As discussed in this Directive, the purchase of parts that do not replace an item that was a component of the qualifying truck or trailer do not qualify for exemption from sales or use tax.

SPECIAL TAXES AND ASSESSMENTS

MOTOR FUEL, IFTA/MOTOR CARRIER, SEVERANCE, TOBACCO, STATE REAL ESTATE TRANSFER, AND HEALTH INSURANCE CLAIMS ASSESSMENT

The purpose of this section is to provide tax preparers with instructions concerning licensing; taxable or nontaxable transactions; special reporting and tax payment procedures; and the rights and responsibilities of the parties involved in motor fuel, motor carrier, tobacco, state real estate transfer tax and health insurance claims assessment transactions. This section is **not** intended to be all-inclusive, but rather to provide general information.

Specific questions concerning motor fuel, motor carrier, severance, tobacco tax licensing, and tax reporting requirements should be directed to Michigan Department of Treasury (Treasury), Bureau of Tax Policy, Special Taxes Division. Write to:

Michigan Department of Treasury
Bureau of Tax Policy - Special Taxes Division
P.O. Box 30474
Lansing, Michigan 48909-7974

<u>Taxing Unit</u>	<u>Telephone</u>	<u>Fax</u>
International Fuel Tax Agreement (IFTA) Motor Carrier	(517) 636-4580	(517) 636-4593
Motor Fuel/Severance	(517) 636-4600	(517) 636-4593
Tobacco	(517) 636-4630	(517) 636-4631

Frequently asked questions and other information can be found on Treasury's Web site at www.michigan.gov/taxes. Click on the Fuel and Tobacco Tax link.

Specific questions regarding the Health Insurance Claims Assessment (HICA) should be directed to Michigan Department of Treasury, Business Taxes Division – HICA. Write to:

Michigan Department of Treasury
Business Taxes Division – HICA
P.O. Box 30427
Lansing, MI 48909

<u>HICA</u>	<u>Telephone</u>	<u>Fax</u>
Quarterly Payments, Annual Return, General Information	(517) 636-4450	(517) 636-4378

Technical questions regarding the HICA Act (517) 636-4357

Frequently asked questions and other information can be found on Treasury's Web site at www.michigan.gov/business taxes.

MOTOR FUEL

LICENSING TYPES

Definitions of Terms Used

Aviation Fuel Registrant. A person who purchases aviation fuel for resale must be registered with Treasury. An Aviation Fuel Registrant is required to pay the aviation fuel tax at the time of purchase. No tax return is required.

Blender. A Blender produces blended motor fuel outside of the bulk transfer/terminal system in Michigan. A person must be licensed as a Blender if he or she blends a taxable product with a non-taxable product below the rack. A person must also be licensed as a blender if he or she blends diesel fuel and biodiesel or ethanol and gasoline below the rack. Blenders must file monthly tax returns.

Bonded or Occasional Importer. A Bonded or Occasional Importer imports motor fuel from outside the United States by transport truck, tank wagon, pipeline, or marine vessel for delivery into a storage facility other than a qualified terminal. The Importer must be licensed in the Canadian Province or Territory, or foreign country from which the fuel is imported. Importers must also be licensed in Michigan and file quarterly tax returns.

Carrier. A Carrier operates a pipeline or marine vessel engaged in the business of transporting motor fuel above the terminal rack. While Treasury does not issue a physical document (license) to these accounts, they must be registered with Treasury and file monthly tax returns.

Exporter. An Exporter exports motor fuel from Michigan to another state or country. The Exporter may be required to be licensed in the other state or province. Exporters must be licensed in Michigan and file quarterly tax returns.

LPG Dealer. A Liquefied Petroleum Gas (LPG) Dealer is a person who sells or delivers LPG into a permanently attached fuel supply tank of a motor vehicle, exchanges or replaces the fuel supply tank of a motor vehicle, or who delivers LPG into storage that is devoted exclusively to the storage of LPG to be consumed in motor vehicles on public roads or highways, or withdraws LPG from the cargo tank of a truck trailer or semi-trailer for the operation of a motor vehicle on public roads or highways of this State, whether used in vapor or liquid form. LPG Dealers must be licensed and file quarterly tax returns.

Permissive Supplier. A Permissive Supplier is a position holder in a terminal outside of Michigan, or one who acquires fuel from a position holder in a terminal outside of Michigan in a two-party exchange and is registered under Internal Revenue Code (IRC) Section 4101. A Permissive Supplier must be licensed and file monthly tax returns.

Position Holder. A Position Holder is a person who has a contract with a terminal operator for the use of storage facilities and other terminal services for motor fuel at the terminal. A Position Holder is the owner of the fuel in the terminal and may or may not be the terminal operator. A Position Holder must be licensed and file monthly tax returns.

Retail Marine Diesel Dealer. A Retail Marine Diesel Dealer sells or distributes diesel fuel to an end user in Michigan for use in boats or other marine vessels. Retail Marine Diesel Dealers must be licensed and file quarterly tax returns.

Supplier. A Supplier is a position holder in a terminal or refinery in Michigan and is registered under IRC Section 4101 for motor fuel transactions in the bulk transfer/terminal system; is a position holder in a terminal or refinery outside of Michigan from which fuel is removed and delivered to Michigan; is a person who acquires fuel at a terminal or refinery in Michigan from a position holder in a two-party exchange; or is a person who imports fuel grade ethanol or produces alcohol or alcohol derivative substances in Michigan or outside of Michigan for delivery to a terminal in Michigan, or acquires alcohol or alcohol derivative substances upon importation. **Biodiesel producers must license as Suppliers.** Suppliers must license and file monthly tax returns.

Tank Wagon Operator - Importer. A Tank Wagon Operator - Importer imports motor fuel from a bulk plant in another state by tank wagon (or transport truck). A Tank Wagon Operator - Importer must be licensed and file quarterly tax returns.

Note: A person may purchase fuel from a Michigan licensed Supplier or Permissive Supplier outside of this State for delivery to Michigan and pre-pay the Michigan motor fuel tax to that Supplier or Permissive Supplier without an Importer license.

Terminal Operator. A Terminal Operator owns, operates, or controls a terminal. All facilities in this State that produce motor fuel and distribute the fuel from a rack, for purposes of Public Act (PA) 403 of 2000, are considered a terminal and shall obtain a Terminal Operator license and file monthly tax returns and an annual reconciliation return.

Transporter. A Transporter is an operator of a railroad or rail car, tank wagon, transport truck, or other fuel transportation vehicle engaged in the business of transporting motor fuel for another person into or out of Michigan below the terminal rack. A Transporter must be licensed and file quarterly tax returns.

GENERAL LICENSING INFORMATION

Application

Applicants must file forms *Motor Fuel Tax License Application* (Form 3712), *Trading Partner Agreement* (Form 3999), and *Electronic Filing Application* (Form 4099). Financial statements are required for Terminal Operator, Supplier, Permissive Supplier, and Bonded or Occasional Importer licenses. License fees are listed on the license application. Once issued, a license remains in effect unless or until it is discontinued by the licensee, or revoked, canceled, or suspended for cause by Treasury. Although the license does not need to be renewed annually, Treasury may, at any time, request that a licensee provide updated information including, but not limited to, financial statements.

Account Number

The licensee's account number is the licensee's Federal Employer Identification Number (FEIN). If a licensee does not have an FEIN, Treasury will issue a Treasury (TR) number. A Michigan Establishment (ME) number will be issued if the licensee is filing tax returns or receiving mail at more than one location.

Bonding

Suppliers, Terminal Operators, and Bonded Importers **must** submit surety bonds unless they provide proof of financial responsibility and there are no indications of risk to the State of Michigan.

If bonding is required, Treasury will notify the licensee in writing and will specify the amount of the bond required. A bonding company licensed to do business in Michigan must issue the bond. It is the responsibility of the licensee to locate a bonding company. In lieu of a surety bond, Treasury may accept a cash bond. Any questions on bonding should be directed to the Special Taxes Division, Motor Fuel Unit, at (517) 636-4600.

Licenses

Licenses are not transferable. Written notice must be provided to Treasury within 30 days if there is a change of at least 20 percent of beneficial ownership. Treasury will advise as to whether a new license is required.

If a business is sold, discontinued, or transferred, written notification must be provided to Treasury within three business days.

Within **15 days** after the discontinuance, sale, or transfer of a business, or the cancellation, revocation, or termination of a license, the licensee shall provide Treasury with a final return and shall include with the return a payment of all motor fuel taxes, penalties, and interest due.

FUEL TAX REPORTING INFORMATION

Most motor fuel returns must be filed electronically. Returns filed electronically must be transmitted by the due date. Electronic payments must generally be initiated the day prior to the due date to be received timely. For licensees who are not required to file electronically, returns, with full payment, are due on the 20th of the month following the close of the reporting period. For example, if a quarterly return reporting period is from January 1 through March 31, the return is due on April 20. If the 20th falls on a weekend or a legal holiday, the return is due on the next business day. If the U.S. Postal Service postmark is dated on or before the due date of the return, the return is considered timely filed.

Tax returns must be filed even if no tax is due. Failure to file will result in Treasury issuing computed assessments against a licensee's account.

Detailed instructions are provided with all tax returns and schedules. **The instructions should be read carefully prior to filling out the returns and schedules.** When preparing returns and schedules, it is imperative that the appropriate product codes be used, including codes for fuel grade ethanol, methanol, gasohol, biodiesel, biodiesel blends, and dyed diesel/biodiesel fuels.

Suppliers, Permissive Suppliers, and Terminal Operators are required to file returns electronically. Suppliers and Permissive Suppliers are required to pay the tax due on their returns by either Automated Clearing House (ACH) debit or credit. Applications are available on the Motor Fuel Web site. Other licensees may be required to file fuel tax returns electronically if they have received timely notice as required by Michigan Compiled Law (MCL) 207.1068 (4). Additional electronic filing information can be found at www.michigan.gov/motorfuelefile.

Tax Return Filing Schedule

Carriers	Monthly
Terminal Operators*	Monthly and Annually
Suppliers	Monthly
Permissive Suppliers	Monthly
Blenders	Monthly
Bonded Importers**	Quarterly
Occasional Importers***	Quarterly
Tank Wagon Operator Importers	Quarterly
Retail Marine Diesel Dealers	Quarterly
Transporters	Quarterly
Exporters	Quarterly
LPG	Quarterly

- * Monthly informational reports are filed by terminal operators. The annual report is a reconciliation report and payment is due on any discrepancies.
- ** Bonded Importers file monthly estimated payments with *Motor Fuel Tax Payment/Proposed Adjustments Coupon* (Form 4020) and then file a quarterly return to reconcile all activity for the reporting quarter.
- *** Occasional Importers must remit tax on each load imported from outside the United States within three business days after either the date the taxable fuel was delivered into Michigan or the date that a valid import verification number was obtained from Treasury, whichever is earlier. *Three Day Payment Voucher* (Form 3778) must accompany the payments. The quarterly return is filed to reconcile all activity for the reporting quarter.

An original or amended return resulting in a refund due the licensee must be filed within four years from the due date of the original return. Refunds for motor fuel used in an exempt manner as described in MCL 207.1032 – 207.1045 must be filed within 18 months of the date of purchase and meet the requirements in MCL 207.1048.

A return resulting in a deficiency will be assessed for a period of four years from the due date of the return or the date the return was filed, whichever is later.

Penalty and Interest

PA 403 provides for both civil and criminal penalties for violations of the act. Penalty and interest for late payment of the tax are charged per the provisions in PA 122 of 1941, as amended.

GENERAL INFORMATION

Alcohol

Alcohol means fuel grade ethanol or a mixture of fuel grade ethanol and another product. Alcohol is included in the definition of gasoline and is to be reported and taxed in the same manner and at the same time as gasoline. Alcohol is subject to tax regardless of whether or not it has been blended with gasoline or other gasoline products unless an exception has been provided for in the Motor Fuel Tax Act. If alcohol upon which tax has been paid is used for a nontaxable purpose, the end user may file a claim for refund. Specific information related to the filing of refund claims can be found on Treasury's Web site at www.michigan.gov/business/taxes. Click on the Motor Fuel Tax link, then the Motor Fuel Tax Refund link.

The amendments to PA 403 of 2000, effective April 1, 2003, remove methanol from the definition of alcohol. The definition of gasoline includes alcohol, and methanol that is sold for blending with gasoline or for use on the road.

Bad Debt Deduction for Licensed Suppliers

Licensed Suppliers are entitled to a credit against the tax due on their return when they have remitted tax that was not ultimately collected from an eligible purchaser, presuming the tax has remained uncollected for 90 days after the date the eligible purchaser should have paid the tax.

The Supplier must advise Treasury in writing of a failure to collect the tax within ten days of the date the eligible purchaser should have paid the tax to the Supplier.

Credit must be claimed on the first return filed by the Supplier after the 90-day period has expired. The claim must identify the defaulting eligible purchaser and be accompanied by any documentation Treasury requires.

If the Supplier subsequently collects any tax from the eligible purchaser for which credit has been claimed, the Supplier is required to remit the tax on the return filed for the period during which the payment was received. The Supplier must provide a statement of explanation that identifies the period for which the tax was paid and any other information or documentation Treasury requires.

Dyed Diesel/Biodiesel Fuel

Dyed diesel/biodiesel fuel is exempt from the motor fuel tax unless it is used for taxable purposes.

Persons licensed as Terminal Operators, Suppliers, Permissive Suppliers, Occasional, Bonded or Tank Wagon Operator Importers, Exporters, Transporters, and Carriers are required to report the removal, importation, or exportation of dyed diesel/biodiesel fuel even though it is not taxable in most cases.

Retail Marine Diesel Dealers must be licensed and file quarterly fuel tax reports. Dyed diesel/biodiesel fuel can be used in marine vessels; however, the tax must be collected and reported on transactions which are not exempt.

Note: It is against both State and federal law to operate a motor vehicle on the public roads of this State using dyed diesel fuel.

Eligible Purchaser

An eligible purchaser meeting the requirements in MCL 207.1075 may delay payment of the motor fuel tax to the Supplier to one business day before the tax is due to Treasury as described in MCL 207.1074.

Exports

Although PA 403 imposes tax on motor fuel upon importation or removal across a terminal rack, there are some situations in which the fuel is exported where the tax does not apply.

Licensed Suppliers are not required to remit Michigan motor fuel tax when they remove fuel across a terminal rack in Michigan for delivery to a location outside of Michigan **if they are licensed for motor fuel tax in the destination state**. Licensed Suppliers who sell fuel at a rack in Michigan to other licensed Suppliers for immediate export are not required to collect tax from the licensed Supplier to whom they are selling **if the Supplier purchasing the fuel is licensed for motor fuel tax in the destination state**.

Suppliers who sell motor fuel to Exporters licensed with Treasury or to other persons for immediate export are **not** required to collect the Michigan motor fuel tax **if proof of export is available in the form of a terminal-issued shipping paper, and the Supplier has pre-collected the destination state tax**.

Not all states have the statutory provisions to allow pre-collection of their tax by Suppliers. If motor fuel is sold by Michigan Suppliers to licensed Exporters or other persons for delivery to a state that does **not** allow pre-collection, the **Michigan tax must be charged**. Suppliers are required to issue, or instruct the terminal operator to issue, shipping papers that meet the requirements listed in MCL 207.1103(d) indicating the state to which the fuel is to be delivered and specifying that Michigan tax has been paid or accrued by the Supplier. If the purchaser subsequently pays tax to the destination state, the purchaser may submit proof to Treasury and request refunds of the Michigan motor fuel tax using the refund claims process.

There are also instances where the destination states do not impose tax on a particular type of fuel that is being purchased for export to their state. When this occurs, Suppliers will **not** charge the Michigan motor fuel tax **if the purchaser is a licensed Exporter**. The Suppliers must issue, or instruct the terminal operators to issue, shipping papers that meet the requirements listed in MCL 207.1103(d) indicating the state to which the fuel is to be delivered, specifying the delivery is subject to the statutory requirements of the destination state, and Michigan tax has **not** been paid or accrued. **If the purchaser is not licensed with Treasury as an Exporter, the Suppliers must charge the Michigan tax**.

Fuel Diversions

PA 403 requires payment of the tax when fuel is diverted to Michigan from its original state of destination. The act further provides for refunds under certain circumstances when fuel is diverted from Michigan to a location outside of this State. In either instance, specific requirements must be met.

Fuel Diversion Numbers

When fuel is diverted from its original state of destination, the owner of the fuel, or the shipper if other than the owner, must obtain a fuel diversion number no later than the next business day after the diversion takes place. An owner can register to report future diversions of Michigan tax-paid fuel to another state or Canada or fuel diverted to Michigan by going to www.trac3.net, clicking on Registration, and entering the required company information. The company identification information only has to be entered once. Information can be verified by clicking on the Confirm option.

Because Internet access may be limited at certain times, Treasury can be called for a diversion number during regular business hours at (517) 636-4600. Regular business hours are Monday through Friday, 8 a.m. through 4:30 p.m.

Diversions-In

Importers are required to report and pay tax on fuel diverted to Michigan when the shipping paper indicates a different state of destination.

Licensed Bonded Importers must remit tax on fuel diverted from an original state of destination other than Michigan to a location in Michigan on Form 4020. The transactions are then reported quarterly on *Fuel Importer Return* (Form 3992).

Licensed Occasional Importers must remit tax on diverted fuel within three business days on Form 3778. The transactions are then reported quarterly on Form 3992.

Licensed Tank Wagon Operator-Importers must report the transactions on Form 3992 and remit tax on Form 4020.

When **unlicensed** importers divert fuel to Michigan from the original state of destination, payment is required within three business days after the date taxable fuel is delivered into Michigan. The collection cost allowance is **not** available.

Licensed Exporters who divert fuel from its original state of destination to Michigan must also pay the tax within three business days after the date the taxable fuel is delivered into Michigan. Again, the collection cost allowance is **not** available.

If an Importer or licensed Exporter purchased the diverted fuel from a Michigan licensed Supplier, the Importer or licensed Exporter may enter into an agreement with the Supplier to have the Supplier collect and remit the tax. The agreement must include, at a minimum, the names of the parties to the agreement, the date the agreement was made, the fuel type, and the number of gallons of fuel. The Supplier must fax or mail a copy of the agreement to Special Taxes Division, Motor Fuel Unit, by the due date of the return period in which the diversion took place.

Diversions-Out

Exporters may seek a refund of the Michigan motor fuel tax, less the collection cost allowance, when tax-paid fuel originally destined for Michigan is diverted to a location outside of this State. Licensed and unlicensed exporters must submit a written request for refund along with a copy of the diversion, invoice, bill of lading, and proof of destination state tax paid.

The Exporter is required to obtain a fuel diversion number by the next business day after the diversion takes place.

Fuel Imported From Outside the United States

If motor fuel upon which tax was not prepaid to a Michigan licensed Supplier or Permissive Supplier is to be imported from another country, an import verification number **must** be obtained from Treasury within 24 hours **before entering** Michigan for each load imported. The person bringing the fuel into Michigan from another country must call the toll-free line at 1-888-213-0676 to obtain the import verification number. The line is available 24 hours a day, 7 days a week.

Note: If a person diverting fuel into Michigan has obtained the required fuel diversion number, the person need not contact Treasury for an import verification number.

Bonded Importers are required to remit **monthly estimated tax payments** with Form 4020 or by Electronic Funds Transfer (EFT) on or before the 20th day of the month following the close of the previous month. A quarterly return must then be filed to reconcile activity for the full reporting quarter. The estimated payments are deducted from the calculated tax due on the return. The quarterly return is due on the 20th of the month following the close of the reporting quarter.

Occasional Importers are required to remit tax on fuel imported from outside the United States on Form 3778 within three business days after the date taxable fuel is delivered into Michigan or after the date the valid import verification number is obtained from Treasury, whichever is earlier. A quarterly return is then filed to reconcile all activity for the full reporting quarter. Payments are deducted from the calculated tax due on the return. The quarterly return is due on the 20th of the month following the close of the reporting quarter.

Invoicing

Motor fuel retailers should properly invoice the sales of motor fuel. Proper invoicing facilitates the customers' ability to file refund claims and prepare any fuel tax returns that may be due.

A properly prepared invoice should contain the following information:

1. Seller's name, address, and account number (FEIN, TR, or ME)
2. Date of sale
3. Name of purchaser. For motor carrier fuel tax purposes, if the purchaser is in a lease agreement, a receipt will be accepted in either name (lessor or lessee), provided a legal connection can be made between the parties
4. Type of fuel sold
5. Number of gallons sold
6. Motor fuel tax rate charged to the customer
7. Signature of the purchaser or purchaser's agent and the seller or seller's agent
8. Invoices must be prepared in duplicate, with the original invoice furnished to the purchaser and the copy kept by the seller for four years.

Invoicing Tax-Exempt Undyed Diesel/Biodiesel Fuel Sales

Undyed tax-exempt diesel/biodiesel retail fuel sales are limited to 100 gallons or less per transaction. If more than 100 gallons are purchased, the tax must be charged and the purchaser must file a claim for refund if the fuel is consumed in a nontaxable manner. It is important to note the claim for refund must be filed within **18 months** from the date of purchase of the motor fuel.

A properly prepared invoice for tax-exempt sales of diesel/biodiesel fuel in quantities of 100 gallons or less must include the following:

1. Seller's name, address, and account number (FEIN, TR, or ME)
2. Date of sale
3. Name of purchaser
4. Descriptions of tax-exempt sale (e.g., home heating, non-highway equipment, etc.)
5. Type of fuel sold
6. Number of gallons sold
7. Price per gallon, including the full tax rate
8. A separate line showing a credit for the Michigan motor fuel tax charged in item 7 above or a statement that **no Michigan motor fuel tax is included in the price per gallon**

9. Signature of the purchaser or purchaser's agent and the seller or seller's agent
10. Invoices must be prepared in duplicate, with the original invoice furnished to the purchaser and the copy kept by the seller for four years.

Record Keeping

Shipping Papers

Refineries, terminal operators, and operators of bulk plants, with the exception of bulk plant operators who deliver into tank wagons, must issue **automated machine-generated** shipping papers. The papers are to be provided to the driver of the fuel transportation vehicle or operator of a train pulling a rail car transporting fuel, and must include all of the following:

1. Address and terminal number of the facility from which the fuel is removed or the address of the bulk plant from which the fuel is withdrawn
2. Date the fuel is removed or withdrawn
3. Gross **and** net gallons removed or withdrawn
4. State of destination as represented by the transporter, shipper, or shipper's agent
5. Notices required by PA 403. MCL 207.1103, 1112, and 1113 impose requirements for the placement of notices on shipping papers (e.g., Dyed Diesel Fuel, Nontaxable Use Only, Penalty for Taxable Use).

When unforeseen circumstances prevent the issuance of automated machine-generated shipping papers, the refinery, terminal, or bulk plant operator may issue a manually prepared shipping paper provided the following requirements are met:

- The refinery, terminal, or bulk plant operator is required to contact Treasury to obtain a Service Interruption Authorization Number, which will be valid for a period of not more than 24 hours. If the cause of the service interruption is not corrected within 24 hours, the refinery, terminal, or bulk plant operator must contact Treasury for another number. The toll-free number to call is 1-888-213-0676. The automated telephone system is available 24 hours a day, 7 days a week.
- The Service Interruption Authorization Number must be included on the shipping papers.

Shipping papers must be maintained at the delivery location for a 30-day period.

All records must be kept for a period of four years from the due date of the return or the date the return was filed, whichever is later. These records may be kept at the delivery location or another business location of the licensee.

Accurate and complete records of all transactions must be maintained for no less than four years.

Right to Examine Records

Treasury has the authority to audit and examine records, books, papers, and equipment of any person including, but not limited to, licensees and bulk end users to ensure that the tax imposed by PA 403 has been paid.

At the request of Treasury, the person is required to make the records, books, or papers available at the person's place of business in Michigan, or at Treasury's location if the records are maintained at a location outside of this State, within three business days.

Failure to comply may result in civil and/or criminal penalties.

RETAIL MARINE DIESEL DEALERS

Retail Marine Diesel Dealers are required to license and file quarterly fuel tax returns. Retail Marine Diesel Dealers can purchase undyed diesel/biodiesel fuel tax paid. Dyed diesel/biodiesel fuel can be purchased tax free but tax is due on the quarterly returns for all fuel sold to non-exempt entities.

The Natural Resources and Environmental Protection Act (PA 451 of 1994) imposes a privilege tax on all gasoline and diesel fuel sold in Michigan which is used to generate power for the operation or propulsion of vessels on the waterways of this State.

Diesel fuel consumed in the watercraft cited below is exempt from the marine waterways tax:

- Watercraft used for commercial fishing
- Watercraft used by Sea Scouts
- Watercraft used in interstate or foreign commerce
- Watercraft used by the Federal, State, or Local Government
- Watercraft owned by a railroad or railroad car ferry company
- Watercraft used in trade, including watercraft used in connection with an activity which constitutes a person's chief business or livelihood.

It is the responsibility of the Retail Marine Diesel Dealer to collect the marine diesel/biodiesel fuel tax from any vessel that is not exempt from the tax, whether the fuel is dyed or undyed diesel/biodiesel fuel.

Who Must Be Licensed as a Retail Marine Diesel Dealer

A licensed Retail Marine Diesel Dealer is any person who engages in the business of selling or distributing diesel/biodiesel motor fuel into boats or other marine vessels or into the bulk storage of an unlicensed end user of marine fuel.

General Information on Marine Retail Sales of Motor Fuel

PA 451 imposes tax on fuel used in vessels on the waterways of this State at the same rate as the tax imposed under PA 403. PA 451 further requires that the tax be collected in the same manner and at the same time as PA 403.

PA 403 prohibits the use of dyed diesel/biodiesel fuel on the public roads and highways of this State; however, it does not prohibit the use of dyed diesel/biodiesel fuel in marine vessels.

Dyed diesel/biodiesel fuel is exempt from the tax under PA 403 so Retail Marine Diesel Dealers can acquire dyed diesel/biodiesel fuel without payment of the tax to their fuel supply source. If untaxed dyed diesel/biodiesel fuel is sold for a taxable purpose, Retail Marine Diesel Dealers must collect the marine fuel tax from the customer and remit the tax with the return.

A Retail Marine Diesel Dealer cannot take credit for dyed diesel/biodiesel fuel acquisitions on the returns, as the fuel supply source should not have charged the tax.

A Retail Marine Diesel Dealer can also acquire undyed diesel/biodiesel fuel. If undyed diesel/biodiesel fuel is acquired, the Retail Marine Diesel Dealer must pay the full tax rate to the fuel supply source.

When sales of undyed diesel/biodiesel fuel are made, the Retail Marine Diesel Dealer will receive a credit on the return for the tax paid to the fuel supply source.

Tax-free sales of undyed diesel/biodiesel fuel into marine vessels are limited to 100 gallons per sale. If more than 100 gallons of undyed diesel/biodiesel fuel is delivered into a vessel, the tax must be charged. The purchaser, if eligible, may file a claim for refund of the motor fuel tax.

Invoicing Tax-Exempt Sales of Marine Diesel/Biodiesel Fuel

A properly prepared invoice for tax-free sales of marine diesel/biodiesel fuel, whether dyed or undyed, must contain the following information:

1. Seller's name, address, and account number (FEIN, TR, or ME)
2. Date of sale
3. Name of purchaser
4. Type of tax-exempt sale (e.g., Sea Scouts, commercial fisherman, etc.)
5. Type of fuel sold (dyed or undyed diesel or biodiesel)
6. Number of gallons sold
7. Price per gallon including tax

8. A separate line showing a credit for the waterways tax charged in item 7 above or a statement that **no Michigan motor fuel tax is included in the price per gallon**
9. Signature of the purchaser or purchaser's agent and the seller or seller's agent
10. Invoices must be prepared in duplicate, with the original invoice furnished to the purchaser and the copy kept by the seller for four years.

Returns and Schedules

A licensed Retail Marine Diesel Dealer may file the following forms electronically using Web direct fillable forms or on paper:

Retail Marine Diesel Dealer Tax Return (Form 3769)

Retail Marine Diesel Dealer Schedule of Receipts (Form 3767)

Retail Marine Diesel Dealer Schedule of Disbursements (Form 4429)

LPG DEALERS

The use of LPG in a highway vehicle upon the roads and highways of this State is taxable under the provisions of PA 403.

Definitions of Terms Used

Liquefied Petroleum Gas. Gases derived from petroleum or natural gases which are in the gaseous state at normal atmospheric temperature and pressure, but which may be maintained in the liquid state at normal atmospheric temperature by suitable pressure. LPG includes those products predominately composed of propane, propylene, butylene, butane, and similar products.

LPG Dealer. A person who is licensed under the requirements listed in MCL 207.1153 to use LPG.

Use, Used, or Uses. Means any of the following:

1. Selling or delivering LPG not otherwise subject to tax under this act, either by placing it into a permanently attached fuel supply tank of a motor vehicle or exchanging or replacing of the fuel supply tank of a motor vehicle.
2. Delivery of LPG into storage devoted exclusively to the storage of LPG to be consumed in motor vehicles on the public roads or highways.
3. Withdrawing LPG from the cargo tank of a truck, trailer, or semi-trailer for the operation of a motor vehicle upon the public roads and highways of this State, whether used in vapor or liquid form.

Who Must Be Licensed as an LPG Dealer

Persons who must be licensed as LPG Dealers are those who perform any of the operations as outlined in the “Definition of Terms Used” section (above) under the terms “Use, Used, or Uses.”

Returns and Schedules

A licensed LPG Dealer must file the following form electronically using a Web direct fillable form or on paper:

Dealer’s Liquid Petroleum Gas Tax Return (Form 577)

IFTA MOTOR CARRIER TAX

GENERAL INFORMATION

Interstate motor carriers are regulated under the Motor Carrier Fuel Tax Act (PA 119) and the International Fuel Tax Agreement (IFTA).

Intrastate motor carriers are not required to license or report for fuel tax purposes.

The IFTA is an agreement between all of the contiguous states in the U.S. and most Canadian provinces.

Under the IFTA, motor carriers file a fuel tax license application with their base jurisdiction and the base jurisdiction issues the motor carrier credentials. Credentials consist of a cab card (license) and a set of decals for each power unit. Credentials are valid for licensing purposes in all participating IFTA jurisdictions through the end of the calendar year in which they are issued. Credentials must be renewed annually.

The IFTA motor carrier files quarterly returns with the base jurisdiction, reporting fuel purchases and miles traveled in all jurisdictions.

WHAT’S NEW

The U.S. Customs Service granted Class 9 Customs Bonded Warehouse status effective September 5, 2000, to the Ammex, Inc. facility adjacent to the Ambassador Bridge at 3400 W. Lafayette, Detroit, Michigan.

Recent court decisions granted the Ammex, Inc. facility the right to sell gasoline and diesel fuel tax free, effective September 5, 2000, when they were granted their current status.

Diesel fuel purchased at the Ammex, Inc. facility does not include the Michigan fuel tax and may not be claimed as a tax-paid purchase on the IFTA return.

Dyed Diesel Fuel

The use of dyed diesel fuel in vehicles on the public roads and highways of this State is prohibited and violators are subject to severe penalties.

A motor carrier may designate a bulk storage tank for dyed diesel fuel for use in off-road equipment. The motor carrier is required to keep a log of fuel disbursements from this tank. This log must have the date of the disbursement, gallons disbursed, and the identification of the equipment being fueled.

Refunds for Non-Highway Use

MCL 207.1045 provides for a refund of fuel tax paid on undyed diesel fuel consumed in **attached equipment**. The statute defines attached equipment as equipment used by the end user in the regular course of his or her business that is powered by diesel fuel from the common fuel supply tank. Attached equipment includes, but is not limited to, certain pumping, spraying, seeding, spreading, shredding, lifting, winching, dumping, cleaning, mixing, processing, and refrigeration equipment. Attached equipment does not include a heater, air conditioner, radio, or any other equipment that is used in the cab of the motor vehicle and does not include any other equipment that Treasury reasonably determines does not meet this definition.

To qualify for the attached equipment refund, vehicles must be exclusively used for business or commercial purposes. The refund does not apply to automobiles even if they are used for business or commercial purposes.

The attached equipment refund is limited to 15 percent of the tax paid on fuel consumed in highway vehicles that qualify for the refund. If claimants believe that a different percentage should be allowed, they should contact the Special Taxes Division, IFTA Tax Unit, for instructions.

The refund must be claimed within 18 months from the date of the fuel purchase.

Notes: There are no provisions in the Motor Carrier Fuel Tax Act or the IFTA Articles of Agreement for the non-highway use of motor fuel in a highway vehicle. The attached equipment refund provisions are found in Michigan’s Motor Fuel Tax Act (PA 403 of 2000). The attached equipment claim for refund is strictly a Michigan provision and consideration for attached equipment cannot be taken on the IFTA fuel tax return.

A motor carrier cannot adjust the IFTA fuel tax returns for fuel consumed in attached equipment. This includes, but is not limited to, the “Taxable Miles” and “Taxable Gallons” columns on the IFTA fuel tax return.

Questions concerning motor carrier licensing and tax reporting requirements or attached equipment refunds can be e-mailed to *IFTA_licensing@michigan.gov*, or write to Treasury at:

Michigan Department of Treasury
Special Taxes Division – IFTA Tax Unit
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The Special Taxes Division, IFTA Tax Unit, may also be contacted at (517) 636-4580 or fax number (517) 636-4593.

Who Must Be Licensed as an IFTA Motor Carrier

Persons operating interstate “qualified motor vehicles” must be licensed as IFTA motor carriers. IFTA defines a “qualified motor vehicle” as a motor vehicle used, designed, or maintained for transportation of persons or property and:

- Having two axles and a gross vehicle weight or registered gross vehicle weight exceeding 26,000 pounds or 11,797 kilograms; or
- Having three or more axles regardless of weight; or
- Is used in combination when the weight of such combination exceeds 26,000 pounds or 11,797 kilograms gross vehicle or registered gross vehicle weight.

It is important to note that when counting the axles to determine if a vehicle or combination of vehicles qualify for licensing, the axles on the trailing unit are not counted, only the axles on the power unit are counted.

Recreational vehicles are not qualified motor vehicles even if they meet the above requirements.

IFTA Base Jurisdiction

R212 of the IFTA Articles of Agreement defines base jurisdiction as “the jurisdiction where qualified motor vehicles are based for vehicle registration purposes” and:

- “.100 Where the operational control and operational records of the licensee’s qualified motor vehicles are maintained or can be made available; and
- .200 Where some travel is accrued by qualified motor vehicles within the fleet. The commissioners of two or more affected jurisdictions may allow a person to consolidate several fleets that would otherwise be based in two or more jurisdictions.”

IFTA Account Number

The account number for an IFTA motor carrier is the FEIN. If the IFTA carrier does not have an FEIN, the IFTA Articles of Agreement require that the motor carrier use an owner’s, partner’s, or corporate officer’s Social Security number (SSN) for identification purposes. The account number printed on the license and returns will be the FEIN or SSN preceded by “MI” and followed by a fleet designator (usually “00”). If several fleets are involved, the last two digits may be “01,” “02,” “03,” etc.

If an interstate motor carrier does not have an FEIN, Treasury will issue a TR number for general tax purposes; however, this number will not be printed on the license or as the IFTA account number on the tax return. A TR number will only be used for refunds or tax assessments.

IFTA carriers are encouraged to contact the Internal Revenue Service (IRS) to obtain an FEIN if they do not already have one. The IRS can be reached at (800) 829-4933 or on the Web at www.irs.gov.

IFTA New and Renewal Applications

Michigan IFTA Fuel Tax License Application (Form 2823) must be completed by a new applicant, a prior licensee who has been discontinued for more than one quarter, or a current licensee applying for additional decals. To ensure prompt processing of the IFTA application, applicants must complete all sections, including the corporate officer information. Applications with missing information cannot be processed.

Renewal Application for Michigan IFTA Fuel Tax License (Form 3014) will be mailed in October of each year to all IFTA carriers who are currently licensed. The IFTA license year is January 1 through December 31. Renewal applications should be returned as soon as possible to ensure credentials will be received by the carrier on time. There is no fee associated with renewal. **Renewal applications will not be processed unless all required IFTA tax returns have been filed.**

Carriers that do not leave the State or file zero reports for three consecutive quarters may not be renewed. Vehicles that qualify for IFTA licensing cannot legally leave the State without valid IFTA credentials or trip permits.

IFTA Temporary Permits

A **licensed IFTA Motor Carrier** can obtain a temporary permit for a qualified motor vehicle(s). Temporary permits are valid for a period of 30 days. This allows enough time for Treasury to process the motor carrier's request for **additional decals** and for the motor carrier to affix these decals to the vehicle(s). Temporary permits are vehicle-specific and temporarily take the place of the motor carrier's additional decals. To qualify for a temporary permit, the motor carrier **must already be licensed for the tax year**. Temporary permits are **not** issued to applicants who are filing their first application or first renewal application for the tax year.

Trip Permits

A motor carrier located outside of the State of Michigan can get a five-day fuel tax trip permit which allows the motor carrier to operate a "qualified motor vehicle" in Michigan that has **not** been licensed for IFTA fuel tax purposes. These permits are vehicle-specific and valid for five consecutive days. Permits can be obtained from the various permitting services or Treasury. The fee is \$20 per permit plus any fees the permitting service may charge. Michigan limits the purchase of fuel tax trip permits to three per calendar year.

IFTA Grace Period for Licensing

The IFTA license year runs from January 1 through December 31. Renewal applications are due by December 31 each year. A licensed IFTA carrier has until the last day in February of the new license year to **display** that year's decals. While this gives motor carriers a two-month grace period after the license year ends, they are encouraged to apply for the next year's license and decals as soon as possible. Pre-identified applications are mailed to IFTA carriers in the latter part of October. IFTA carriers waiting until December 31 to apply for their next year's license run the risk of not receiving their credentials prior to the expiration of the grace period. This lapse in licensing may result in the motor carrier being cited by law enforcement agencies for not having a current fuel tax license. All activity conducted under the prior year decals must be reported.

Bonding

Treasury may require bonding as a condition of licensing. If bonding is required, Treasury will notify the IFTA carrier in writing and will specify the amount of the required bond. A bonding company licensed to do business in Michigan must issue the bond. It is the responsibility of the motor carrier to locate a bonding company. In lieu of a surety bond, Treasury may accept a cash bond. Any questions on bonding should be directed to the Special Taxes Division, IFTA Tax Unit, at (517) 636-4580.

License Revocation

IFTA carriers may have their licenses revoked if they fail to file IFTA fuel tax returns and pay the tax when due. If an IFTA carrier's license is being reviewed for revocation, Treasury will notify the motor carrier in writing of the time and place for a "show cause" hearing. At this hearing, the IFTA carrier will have the opportunity to discuss the delinquency with Treasury and arrange for corrective action. Failure to appear at the "show cause" hearing or failure to comply with conditions set forth in this hearing will result in the immediate revocation of the IFTA carrier's fuel tax license. Once an IFTA carrier's fuel tax license is revoked, the IFTA carrier, or the IFTA carrier's representative, may not operate the "qualified vehicles" until such time the reason for the revocation has been remedied. If an IFTA carrier does operate a qualified vehicle with a revoked fuel tax license, law enforcement agencies may impound the vehicle. This can become very costly for the IFTA carrier as he or she will be held liable for storage fees and any other fees involved in impounding the vehicle.

IFTA Fuel Tax Returns and Schedules

The following return and schedule must be filed by licensed IFTA carriers:

- *IFTA Quarterly Fuel Use Tax Return* (Form IFTA-100)
- *IFTA Quarterly Fuel Use Tax Schedule* (Form IFTA-101)

The following forms are used in preparing the IFTA fuel tax return:

- *IFTA Final Fuel Use Tax Rate and Rate Code Table* (Form IFTA-105) **(This form is revised quarterly because of tax rate changes in the participating jurisdictions.)**
- *Continuation of The IFTA-105 - IFTA Final Fuel Use Tax Rate and Rate Code Table* (Form IFTA-105.1) **(This form is revised quarterly because of tax rate changes in the participating jurisdictions.)**

Be sure to use the correct rate code tables for the quarterly return being filed. Updated rate codes are available on Treasury's Web site at www.michigan.gov/taxes (click on the Fuel and Tobacco Tax link).

Electronic Filing of IFTA Returns

IFTA carriers are encouraged to file their IFTA returns electronically. Credit and debit electronic EFTs can also be made after an application has been completed and approved. Information is available on Treasury's Web site at www.michigan.gov/iftaefile.

IFTA Record Keeping Requirements

IFTA carriers must keep records of all fuel purchases and mileage. IFTA carriers must report fuel purchases and miles traveled in each jurisdiction. Records must be kept for a minimum of four years from the due date of the return or the date the return was filed, whichever is later.

Farm plated vehicles have special reporting requirements. See the notice on Treasury's Web site at www.michigan.gov/taxes (click on the Fuel and Tobacco Tax link).

Inadequate record keeping is a primary reason why fuel tax deficiencies are discovered in a field audit. If an IFTA carrier fails to keep adequate fuel purchase and mileage records, the statute requires that Treasury adjust the fleet average mileage to four miles per gallon.

Due Date of Return

IFTA returns are due quarterly on January 31, April 30, July 31, and October 31. If the due date of the return falls on a weekend or legal holiday, the return is due on the next business day. If the U.S. Postal Service postmark date is on or before the due date of the return, the return is considered timely filed.

Penalty and Interest Provisions

Penalty is charged pursuant to the IFTA Articles of Agreement R1220. The penalty charge for the first month is \$50 or ten percent of the tax due, whichever is greater. After the first month, IFTA carriers are subject to the penalty provisions in MCL 205.24 for failure to pay taxes in a timely manner.

In addition, Treasury, on a case-by-case basis, may charge discretionary penalties as provided for in MCL 205.23.

Interest is also charged for late payment of tax on a return. R1230 of the IFTA Articles of Agreement provide an annual interest rate of 12 percent for carriers based in U.S. jurisdictions. Canadian IFTA carriers pay a rate equal to the Canadian Federal Treasury Bill rate plus two percent and the rate is adjusted every calendar year.

Interest for IFTA carriers is calculated separately for each jurisdiction. An overpayment in one jurisdiction shall not affect the interest calculation for any other jurisdiction. Because interest is charged on an individual jurisdictional basis and not on the net amount of tax due, the interest can sometimes exceed the amount of tax due.

Lease Agreements

Lease agreements are a common practice in the motor carrier industry. This practice can and does complicate the filing and processing of fuel tax returns. Many IFTA carriers have found themselves facing large tax liabilities because they failed to understand who has the tax reporting responsibility under a lease agreement. The following may assist IFTA carriers in lease situations:

- Before signing a lease agreement, be sure the fuel tax licensing and reporting requirements for both the lessor and the lessee are acknowledged in writing. Too often this is not the case.
- Lessors should not assume the other party is filing the fuel tax returns on their behalf.
- Lessors should cancel their IFTA fuel tax license if they are in a lease agreement where all of the following conditions have been met:
 - Lessee has provided the fuel decals and a copy of the license for the vehicle and the license and decals are in the lessee's name. **If the license and decals are not in lessee's name, contact the Special Taxes Division, IFTA Tax Unit, at (517) 636-4580 for instructions.**
 - Lessee has agreed, in writing, to file for the activity of the lessor on the lessee's fuel tax returns.
 - Lessee has exclusive use of the equipment.
- IFTA licensees are required to file quarterly returns as long as they maintain an active account. This is true even if the licensee is in a lease agreement where another party has provided the credentials and agreed to report all activity. If the licensee is in a long-term lease agreement, the licensee's individual account should be canceled.
- If a licensee decides to maintain an individual account while in a lease agreement, a "no activity" return must be filed. A legible copy of the lease agreement should be attached to the return.
- If no return is filed, estimated assessments will be issued against the licensee.

- The lease agreement should clearly state who has the fuel tax licensing and tax reporting responsibility. If the lessee does not have exclusive use of the equipment, the lessor must account for the use of the equipment when the lessee is not using it. Sometimes equipment has multiple lessees and the lessor must account for the activity of each lessee.
- It is important to remember the lessor and lessee may be held **jointly and severally liable** for any liability created by the operation of the leased vehicle.

Discontinuance of Business

If a motor carrier ceases to engage in business in Michigan, the motor carrier shall notify Treasury in writing within 15 days after discontinuance. When filing a final fuel tax return, the motor carrier should check the box marked “Cancel License.” If the motor carrier fails to check the box, Treasury may issue estimated tax assessments for failure to file fuel tax returns as it is presumed the motor carrier is still operating.

SEVERANCE TAX

General Information

The severance tax is levied upon each producer engaged in the business of severing oil or gas from the soil. The Michigan Severance Tax Act, MCL 205.303, places the responsibility for reporting and paying the severance tax on the producer of Michigan oil and gas. However, the act also requires that if the common purchaser deducts the tax from payments paid to the producer, the common purchaser is required to remit the tax to Treasury.

Key Definitions

Producer. A person who owns or is entitled to delivery of a share in kind or a share of the monetary proceeds from the sale of gas or oil at the time of its production or severance.

Common Purchaser. A purchaser capable of purchasing all of the production in a given area. A common purchaser will have pipelines and gathering lines that enable the purchase of all production in a common area.

Taxpayers are not required to be licensed, but additional information may be required to determine the reporting responsibility for each well.

Monthly tax returns are due on the 25th of each month following the preceding month of production and/or sales of the severed product. Returns not filed by the 25th are subject to the late filing penalty and interest provisions of the Michigan Revenue Act MCL 205.1 et. seq.

Due to the nature of the industry of severing gas and oil from the soil, a taxpayer may elect to file an estimated liability and payment. For more information concerning estimated tax payments, see Revenue Administrative Bulletin (RAB) 1989-14.

Tax Rates

Severance tax rates are:

- Oil: 6.6 percent of gross cash market value
- Oil - Marginal or stripper wells: 4 percent of gross cash market value
- Gas: 5 percent of gross cash market value.

Oil and Gas Fee

There is a maximum fee of 1 percent of the gross cash market value on gas and oil. This fee may vary annually. For the latest fee information, call the Special Taxes Division, Severance Tax Unit, at (517) 636-4600.

Tax Returns and Schedules

All severance tax returns and schedules were revised on January 1, 2008. These forms are:

- *Oil Severance Tax Return* (Form 381)
- *Gas Severance Tax Return* (Form 382)
- *Production Report - Gross Production By Well Schedule* (Form 383)
- *Exempt Production and Value Report By Well Schedule* (Form 384)
- *Gas Storage Field Report* (Form 385).

TOBACCO PRODUCTS TAX

The Michigan Tobacco Products Tax Act, Public Act (PA) 327 of 1993, was amended on January 9, 2009, requiring licensed secondary wholesalers to report all purchases and sales made after January 9, 2009, on a monthly tobacco tax return.

General Information

PA 327 of 1993, as amended, imposes tax upon the consumer of tobacco products; requires certain persons to collect and remit the tax for the consumer; and sets specific requirements for licensing, stamping, collecting, and remitting tax. The act also provides for both civil and criminal penalties for violations.

Tax Rates

Effective July 1, 2004, the tax rate for cigarettes is 100 mills per cigarette. A deduction of 1.50 percent is provided for Wholesalers and Unclassified Acquirers to allow for the cost of remitting the tax on cigarettes.

The tax rate for other tobacco products is 32 percent of wholesale price. A deduction of 1 percent is provided for Wholesalers and Unclassified Acquirers to allow for the cost of remitting the tax on tobacco products other than cigarettes.

Key Definitions

Cigarette. A roll for smoking made wholly or in part of tobacco, irrespective of size or shape and irrespective of the tobacco being flavored, adulterated, or mixed with any ingredient, which roll has a wrapper or cover made of paper or any other material.

Manufacturer. A person who manufactures or produces a tobacco product.

Noncigarette Smoking Tobacco. Tobacco sold in loose or bulk form that is intended for consumption by smoking.

Secondary Wholesaler. A person who sells a tobacco product for resale, who purchases a tobacco product from a wholesaler or unclassified acquirer licensed under this act, and who maintains a nonresidential, secured established place of business in this State where a substantial portion of the business is the sale of tobacco products and related merchandise at wholesale, and where at all times a substantial stock of tobacco products and related merchandise is available to retailers for resale.

Note: Secondary Wholesalers only purchase and sell tax-paid, pre-stamped products.

Smokeless Tobacco. Snuff, chewing tobacco, and any other tobacco that is intended to be consumed by means other than by smoking.

Stamp. A distinctive character, indication, or mark, as determined by Treasury, attached or affixed to an individual package of cigarettes by mechanical device or other means authorized by Treasury to indicate that the tax imposed under this act has been paid.

Stamping Agent. A licensed Wholesaler or Unclassified Acquirer other than a manufacturer who is authorized by Treasury to affix stamps to individual packages of cigarettes on their own behalf, or on behalf of another licensed Wholesaler or Unclassified Acquirer other than a manufacturer.

Tobacco Products. Cigarettes, cigars, non-cigarette smoking tobacco, or smokeless tobacco.

Unclassified Acquirer. A person other than a transportation company or purchaser at retail from a retailer who imports or acquires tobacco products from a source other than a licensed Wholesaler or Secondary Wholesaler for use, sale, or distribution. Also includes a person who receives cigars, non-cigarette smoking tobacco, or smokeless tobacco directly from a manufacturer licensed under the Tobacco Products Tax Act, or from another source outside Michigan who is not licensed under this act. A Wholesaler is not an Unclassified Acquirer. **An Unclassified Acquirer, including a Direct Buy Vendor, is responsible for affixing stamps to individual packages of cigarettes or placing a prescribed marking on shipping containers of tobacco products other than cigarettes, prior to delivery, sale, or distribution, and for remitting tax.**

Note: Direct Buy Vendors purchase some or all of the tobacco products to be placed in their vending machines from manufacturers.

Wholesale Price. The actual price paid for a tobacco product by a Wholesaler to a manufacturer, including any tax, but excluding any discounts or reductions.

Wholesaler. A person who purchases all or part of the tobacco products from the manufacturer, sells 75 percent or more to others for resale, and is required to maintain inventory of Michigan tobacco products at all times. The inventory of tobacco products may be stored in a licensed facility in any state, provided the tobacco products are designated for Michigan inventory at the time of purchase, are segregated from inventory for other states, and written records are maintained. A Wholesaler may also be a chain store retailing tobacco products to consumers if 75 percent of their tobacco products are purchased from manufacturers. **A Wholesaler is responsible for affixing stamps to individual packages of cigarettes or placing a prescribed marking on shipping containers of tobacco products other than cigarettes, prior to delivery, sale, or distribution, and for remitting tax.**

Licensing

Wholesalers, Secondary Wholesalers, Transporters, Transportation Companies, and Unclassified Acquirers, including Direct Buy Vendors and manufacturers, must be licensed to report and remit tax, if applicable, directly to the State.

Secondary Wholesalers and Vending Machine Operators, other than Direct Buy Vendors, must be licensed, but may only purchase tobacco products with the tax included. Vending Machine Operators do not file tobacco products tax returns and must obtain vending machine markers to be placed on all machines from which tobacco products are dispensed.

The license year for tobacco products tax is July 1 through June 30. Licenses must be renewed annually. *Tobacco License Application* (Form 336) must be filed to either obtain a new license or to renew a license.

Applicants for new or renewed Wholesaler, Secondary Wholesaler, and Unclassified Acquirer licenses must submit current financial statements, including the balance sheet, income statement, and accountant's notes with their applications. Wholesalers and Unclassified Acquirers may be required to provide surety bonds in amounts to be determined by Treasury.

Applicants for vending machine operator's licenses, either new or renewed, must attach vending machine location lists to their license applications.

First-time applicants are required to submit evidence of a minimum net worth of \$25,000, proof that the applicant owns or leases a secure nonresidential facility for the purpose of receiving and selling tobacco products, proof of United States citizenship or eligibility to obtain employment, and any other information Treasury may deem necessary.

First-time applicants must also submit the following forms:

- *Application For Non-Cigarette Tobacco Products Stamp* (Form 323) (Wholesalers and Unclassified Acquirers of tobacco products other than cigarettes)
- *Stamping Agent Agreement* (Form 3371) (Wholesalers and Unclassified Acquirers of cigarettes who wish to have an agent affix stamps for them, if license application is approved)
- *Trading Partner Agreement* (Form 3999) (Wholesalers, Secondary Wholesalers, and Unclassified Acquirers of Cigarettes and Other Tobacco Products (OTP) who choose to submit the monthly tobacco tax return via ASCII file, if license application is approved)
- *Tobacco Products Electronic Filing Application* (Form 4154) (All Wholesalers, Secondary Wholesalers, and Unclassified Acquirers of Cigarettes and OTP must complete to become authorized to file electronically, if license application is approved)
- *Tobacco Products Electronic Funds Transfer (EFT) Credit Application* (Form 4239). (All Wholesalers and Unclassified Acquirers of Cigarettes and OTP who choose to submit the monthly tobacco tax payment via ACH Credit, if license application is approved) **(A fee may be assessed by the applicant's financial institution.)**
- *Tobacco Products Electronic Funds Transfer (EFT) Debit Application* (Form 4240). (All Wholesalers and Unclassified Acquirers of Cigarettes and OTP who choose to submit the monthly tobacco tax payment via ACH Debit, if license application is approved). **(No fee is assessed for this service.)**

License Fees

Wholesaler	\$100
Secondary	25
Unclassified Acquirer*	
Manufacturer	100
Retail importer/mail order buyer - OTP	10
Retail importer - cigarettes	100
Direct buy vendor	100
Michigan retailer buying OTP	
from out-of-state distributors not licensed in Michigan	
or manufacturers licensed in Michigan*	10
Transportation Company	5
Transporter	50
Vending Machine Operator (other than direct buy vendor)	25

*The act requires importers to be licensed as Unclassified Acquirers and to pay the tax upon importation. Many of the tobacco products other than cigarettes are specialty items for which there is no distributor in Michigan. Retailers are only able to purchase these products from supply sources located outside Michigan. To ensure that tax is remitted, Treasury will license retailers who wish to purchase **tobacco products other than cigarettes** from unlicensed out-of-state distributors or licensed manufacturers as Unclassified Acquirers.

Stamping of Packages of Cigarettes and Shipping Containers of Non-Cigarette Tobacco Products

Licensed Wholesalers and Unclassified Acquirers (or their authorized Stamping Agents) of cigarettes are required to place stamps obtained from Treasury on the bottom of individual packages of cigarettes to be sold within Michigan. The stamp must be in an aggregate denomination equal to the amount of tax applicable to the contents of each package.

Licensed Wholesalers and Unclassified Acquirers (or their authorized Stamping Agents) of non-cigarette tobacco products are required to place a stamped marking on all shipping containers of non-cigarette tobacco products to be sold within Michigan. The stamp must be obtained from Treasury.

The act provides for civil and criminal penalties for noncompliance. Treasury and its authorized agents may seize tobacco products that are not stamped in accordance with the act.

Stamping Agents, who must be licensed Wholesalers or Unclassified Acquirers under the act, may be appointed by licensed Wholesalers or Unclassified Acquirers who do not choose to stamp their own tobacco products. Form 3371 must be filed with Treasury by the person wishing to assign an agent.

Reporting

Treasury has implemented an electronic reporting system. Along with the new system, new forms were developed. The forms may be viewed on Treasury's Web site at www.michigan.gov/tobacco/taxes.

Wholesalers, Secondary Wholesalers, Unclassified Acquirers, and Direct Buy Vendors are required to file monthly tax returns electronically, with full payment of the tax due, if applicable, for sales of tobacco products. The report must account for all tobacco products and stamping activity for each reporting period. Returns are due on the 20th of the month following the close of the report month and must be filed even if no tax is due. Filing instructions are provided with the return forms and schedules or can be obtained by contacting the Special Taxes Division, Tobacco Tax Unit, at (517) 636-4630.

Manufacturers who are only responsible for tax on promotional products for which their customers have not been charged, must be licensed as Unclassified Acquirers and must file a monthly return even if no tax is due. A manufacturer's report, listing all sales to Michigan licensees, must also be filed monthly.

Tobacco Master Settlement Agreement

On November 23, 1998, Michigan signed the Master Settlement Agreement (MSA) along with 45 other states, the District of Columbia, several territories, and a number of tobacco product manufacturers.

Under the MSA, tobacco product manufacturers who signed the MSA agree to deposit funds into an escrow account for subsequent distribution to the settling states. The purpose of the funds is to settle existing and potential suits filed by the states against the tobacco product manufacturers.

On December 28, 1999, the Michigan Legislature enacted PA 244. This act requires that tobacco product manufacturers either participate in the MSA or, as a nonparticipating manufacturer (NPM), deposit funds into an escrow account based on the number of cigarettes sold in each calendar year.

For purposes of PA 244, the definition of "cigarette" includes "roll-your-own" (RYO) tobacco (0.09 ounces of RYO tobacco equals one cigarette).

The definition of "tobacco product manufacturer" under PA 244 includes the manufacturer of cigarettes (including RYO tobacco) intended to be sold in the United States, and the first purchaser for sale within the United States of cigarettes (including RYO tobacco) that were not intended for United States sale.

To determine accurately the number of units of cigarettes (including RYO tobacco) manufactured by NPMs and sold within Michigan, Treasury requires that licensed Wholesalers and Unclassified Acquirers file a monthly Schedule K with their Tobacco Products Tax Return. The Schedule K is used to report the number of cigarette sticks and volume of RYO tobacco acquired or imported, name of the NPM, brand code, and brands of products acquired or imported. Returns to the NPM or exports to other states are also reported and deducted from acquisitions and imports to arrive at the units subject to escrow by the NPM.

Treasury has developed a Web site that provides, directly or by reference to other sites, the names of participating manufacturers and NPMs who have complied with the requirements, as well as other pertinent information related to PA 244 and the MSA. The Web address is www.michigan.gov/tobaccotaxes.

Direct questions about the filing of Schedule K to Special Taxes Division, Tobacco Tax Unit, at (517) 636-4630. Technical questions concerning the MSA and PA 244 should be directed to Bureau of Tax Policy at (517) 373-9600.

THE EQUITY ASSESSMENT PRE-PAYMENT REQUIREMENT

PA 327 of 1993 was amended on January 8, 2004. The amendment required all NPMs who anticipate selling their cigarettes and RYO products in Michigan to pre-pay an equity assessment by February 9, 2004, for 2004 sales. The bill also requires NPMs to make additional annual pre-payments by March 1 of each year, based on the anticipated cigarette and RYO tobacco sales for that calendar year. Treasury will perform a reconciliation of the pre-payment to actual sales by April 15 of each year.

The equity assessment is based on the estimated tobacco sales for the current year or a minimum payment of \$10,000 to be paid prior to commencing selling cigarette and RYO tobacco products into the state of Michigan.

The amendment to PA 327 states that a Stamping Agent shall not affix a State of Michigan stamp to any package of cigarettes or shipping container of RYO tobacco of an NPM unless the manufacturer is listed on Treasury's Web site at www.michigan.gov/tobaccotaxes.

Treasury may seize or confiscate from any person an NPM's cigarettes or RYO tobacco products in that person's possession which are in violation of this act.

ELECTRONIC FILING OF TOBACCO TAX RETURNS

The State offers electronic filing of tobacco tax returns. All current tobacco tax returns have been updated to accommodate electronic filing of the returns.

To obtain current forms, applications to register for electronic filing and/or payment, and to get information regarding electronic filing, visit Treasury's Web site at www.michigan.gov/tobaccotaxes.

STATE REAL ESTATE TRANSFER TAX

P.A. 330 of 1993, enacted the State Real Estate Transfer Tax (SRETT). SRETT applies to written instruments executed within the State, or written instruments executed outside of the State if the contract or transfer evidenced by the written instrument concerns property wholly located within the State. Contracts for the sale or exchange of property or any interest in the property or any combination of sales or exchanges or any assignment or transfer of property or any interest in the property are covered by the SRETT act. "Property" includes land, tenements, real estate, real property and all rights to and interests in land, tenements, real estate, or real property.

P.A. 473 of 2008 amended SRETT effective January 1, 2007 to include the contracts for the transfer or acquisition of a controlling interest in any entity if the real property owned by that entity comprises 90 percent or more of the fair market value of the assets of the entity determined in accordance with generally accepted accounting principles. "Controlling interest" means more than 80 percent of the total value of all classes of stock of a corporation; more than 80 percent of the total interest in capital and profits of a partnership, association, limited liability company, or other incorporated form of doing business; or more than 80 percent of the beneficial interest in a trust. Recording in this case is mandatory.

The person who is the seller or grantor of the property is liable for the tax imposed under the SRETT act. "Person" means an individual, partnership, corporation, limited liability company, association, governmental entity, or other legal entity. The tax imposed under SRETT is payable to the county treasurer where the real property is located not later than 15 days after the delivery of the instrument effecting the conveyance by the seller or grantor to the buyer or grantee or not later than 15 days after the transfer of a controlling interest in any entity with an interest in real property. The date of the instrument effecting the transfer is presumed to be the date of delivery of the instrument.

The tax imposed under the SRETT is at the rate of \$3.75 for each \$500.00 or fraction of \$500.00 of the total value of the property being transferred. "Value" means the current or fair market worth in terms of legal monetary exchange at the time of the transfer. The tax shall be based on the value of the real property transferred and shall be collected at the time the instrument of conveyance is submitted for recording. In the case of controlling interest in any entity that owns real property, value shall mean the value of the real property or interest in the real property, apportioned based on the percentage of the ownership interest transferred or acquired in the entity.

A written instrument subject to the SRETT must state on its face the total value of the real property being transferred unless an affidavit is attached to the written instrument on a form prescribed by Treasury declaring the total value of the real property being transferred. If the sale or transfer is a combination of real and personal property, the tax is applicable only to the transfer of the real property if the values of the real and personal property are stated separately on the face of the written instrument or an affidavit is attached to the written instrument setting forth the respective values of the real and personal property.

The SRETT provides for many exemptions under MCL 207.526 located at www.legislature.mi.gov. An exemption of particular interest is an exemption under MCL 207.526(u). Michigan Attorney General Opinion No. 7214 further explains this exemption located on the Attorney General Web site at www.michigan.gov/ag.

The SRETT is required to be credited to the school aid fund. SRETT is administered by Treasury under the Revenue Act, MCL Sections 205.1 to 205.31.

HEALTH INSURANCE CLAIMS ASSESSMENT

NEW

P.A. 142 of 2011, enacted on September 20, 2011, creates the Health Insurance Claims Assessment (HICA) Act. Beginning January 1, 2012, certain third party administrators, carriers, and self-insured entities are required to pay an assessment on certain paid health care claims. HICA is a successor to the Health Maintenance Organization (HMO) use tax. It is intended to generate funds that will be used to leverage federal Medicaid matching funds. For the majority of filers, the assessment is levied at the rate of one percent of the “paid claims” of the covered carrier, third party administrator, or self-insured entity.

Generally, the Michigan HICA is levied upon:

- Certain insurance carriers
- Self-insured entities
- Employers
- Employee organizations
- Third party administrators that pay health insurance claims for Michigan residents for health-related services performed in Michigan.

The assessment is levied upon the “paid claims” of those entities. (See MCL 550.1732(s).) An organization will be subject to the one percent assessment if they meet the definition of “carrier” or “third party administrator” under the Act. (See MCL 550.1732(s), 550.1732(v).)

However, the assessment is only owed once with respect to any single “paid claim” where more than one entity may be subject to the assessment; such as, an employer and its third party administrator. The statute provides a hierarchy to determine which entity is liable for paying the assessment. (See MCL 550.1733(3).) The HICA does not contain an exemption for filers owing assessment amounts below a certain *de minimis* threshold.

The Act uses the terms “insured individual” and “covered life” (see MCL 550.1733(4)). While these terms are not defined in the Act, an individual person can be an “insured individual” or a “covered life” only with respect to a specific policy or program of insurance coverage. Therefore, Treasury has interpreted this provision to mean that the \$10,000 cap will be applicable per insurer or third party administrator.

For purposes of the HICA, a Michigan “resident” is an individual who is domiciled in the State of Michigan on the date that the service in question is performed. “Domicile” means a place where an individual has his or her fixed, permanent and principal home to which, whenever he or she returns or intends to return. An individual’s domicile in one place continues until a different domicile is established. A rebuttable presumption shall exist that an individual’s home address, as maintained in the ordinary business records of a carrier or third party administrator, indicates the domicile of that individual under this definition. Example: An individual who is domiciled in Michigan, but attends college in another state, is a Michigan resident for purposes of the HICA Act. If that individual obtains health services in Michigan while home between semesters, a “paid claim” for the performance of those services will be subject to the assessment under the HICA Act.

All HICA payments are required to be remitted using EFT. You must register for either EFT Debit or Credit by completing the *Electronic Funds Transfer Application – Health Insurance Claims Assessment* (Form 4926) available on Treasury’s Web site at www.michigan.gov/biztaxpayments. Questions regarding EFT registration or the EFT process should be directed to Treasury’s EFT Unit at (517) 636-6925.

Quarterly payments are due April 30, July 30, October 30, and January 30 of each year and must be made by EFT. *Quarterly Worksheet for Health Insurance Claims Assessment* (Form 4930) is available on Treasury’s Web site to assist in determining the quarterly liability. The worksheet is **not** submitted to Treasury, but should be retained in the HICA filer’s records for a period of four years. If no assessment is owed for the period, a \$0.00 EFT transmission may be sent to complete the filing information for the quarter, but it is not required.

An annual return is required to be filed for each HICA payer registered to make HICA payments, even if no payment is due or no refund is requested. The annual return is due February 28 for the previous assessment year. E-filing the HICA annual return ensures timely processing. The HICA annual return e-file system and related information about the annual return will be available on Treasury’s Web site www.michigan.gov/businessstaxes in November 2012, in advance of the first annual return due date of February 28, 2013.

If a due date falls on a Saturday, Sunday, State holiday for Michigan, or legal banking holiday, the HICA payments and returns are due on the next succeeding business day.

“Paid claims” subject to the assessment are defined, in part, as payments “made to a health and medical services provider.” (See MCL 550.1732(s).) “Health and medical services” is separately and very broadly defined under the Act. (See MCL 550.1732(j).) All of the following are included in the definition of “health and medical services,” and claims based on these services will be subject to the HICA Act assessment:

- Services included in furnishing medical care, dental care, pharmaceutical benefits, or hospitalization
- Ancillary services including, but not limited to, ambulatory services and emergency and nonemergency transportation

- Services provided by physicians (including both M.D.s and D.O.s), nurses, dentists, chiropractors, acupuncturists, audiologists, optometrists, speech-language therapists, pharmacists, physical therapists, podiatrists, psychologist, occupational therapists, dietitians and nutritionists, social workers, and respiratory care therapists
- Behavioral health services, including, but not limited to, mental health and substance abuse services.

Additionally, the term “health and medical services” specifically **excludes** services provided by veterinarians, marriage and family therapists, athletic trainers, massage therapists, licensed professional counselors and sanitarians. (See MCL 550.1732(j)(iii).)

The one percent HICA assessment does not apply to:

1. Payments for services provided before January 1, 2012
2. Claims paid for services provided to persons who are not residents of Michigan
3. Claims paid for services provided outside of Michigan to Michigan residents
4. Claims-related expenses
5. Claims paid under specified accident or accident-only coverage, credit, disability income, long-term care, automobile insurance, homeowners’ insurance, farm owners’ insurance, commercial multi-peril coverage, worker’s compensation, and coverage issued as a supplement to liability insurance.
6. Claims paid under a federal employee health benefit program, Medicare, Medicare Advantage, Medicare Part D, Tricare by the U.S. Veterans Administration and for certain risk pools, and
7. Reimbursements to individuals under a flexible spending arrangement, a health savings account, an Archer medical savings account, a Medicare Advantage medical savings account, or other health reimbursement arrangements authorized under federal law.

The HICA does not address the relationship between an employer and its employees. Other laws, such as contract law and labor law, may govern that relationship, but the HICA itself is silent on this issue. Accordingly, the HICA itself neither permits nor prohibits an employer from passing the cost of the HICA on to its employees.

The HICA defines “carrier” to include an employer or employee organization that establishes or maintains a group health plan. (See MCL 550.1732(a).) However, if a self-insured employer uses a third party administrator to pay its health care claims, under the hierarchy provided under the statute, the third party administrator would be responsible for paying the HICA to Treasury. (See MCL 550.1733(3).)

Under the statute, third party administrators are required to pay the one percent HICA on covered claims that they pay or process, even if the claims are not paid from the assets or bank account of the third party administrator, and instead are funded directly by the third party administrator's client. The definition of "paid claims" under the statute includes payments that are made under a service contract for administrative services only. (See MCL 550.1732(s).)

Note: There is nothing in the language of the HICA that would specifically exempt non-taxable entities from the assessment, as long as they are otherwise a carrier, third party administrator, or self-insured entity under the terms of the Act.

The assessment levied under HICA should be paid by the third party administrator. Both the organization, as a self-insured entity, and the third party administrator are potentially subject to the assessment under the HICA. However, the assessment is only owed once with respect to any single "paid claim." In this case, the statute provides a hierarchy to determine which entity must pay the assessment.

The statute provides that "[a] group health plan sponsor shall not be responsible for assessment . . . for a paid claim where the assessment on that claim has been paid by a third party administrator . . ." (Section 3(2)(a).) The statute further provides that the third party administrator "shall be responsible for all assessments on claims paid by the third party administrator." (Section 3(2)(b).)

In circumstances where two entities may both be subject to the HICA for the same claim, the statute provides a hierarchy to determine which entity must actually pay the one percent assessment. In the case of a third party administrator and a stop loss or excess loss insurer, the statute provides as follows:

"If there is both a third party administrator and an excess loss or stop loss insurer servicing the group health plan, the third party administrator shall be responsible for all assessments for paid claims that are not reimbursed by the excess loss or stop loss insurer and the excess loss or stop loss insurer shall be responsible for all assessments for paid claims that are reimbursable to the excess loss or stop loss insurer." (See MCL 550.1733(3)(d).)

Accordingly, under this provision, the third party administrator will be responsible for the HICA on "paid claims" up to the attachment point (the point at which the stop loss or excess loss coverage begins to apply), and the stop loss or excess loss carrier will be responsible for the assessment on the amount of each "paid claim" that exceeds the attachment point.

While both a health plan sponsor and its third party administrator may be subject to the HICA, the assessment is only owed once with respect to any single "paid claim." The statute provides a hierarchy to determine which entity must pay the assessment. The statute provides that:

"[a] group health plan sponsor shall not be responsible for an assessment . . . for a paid claim where the assessment on that claim has been paid by a third party administrator . . ." (See MCL 550.1733(2)(a).) The statute further provides that the third party administrator "shall be responsible for all assessments on claims paid by the third party administrator." (See MCL 550.1733(2)(b).)

Accordingly, the third party administrator is responsible for paying the HICA with respect to claims it pays on behalf of a group health plan sponsor. Michigan law prohibits Treasury from disclosing taxpayer information to third parties, except in certain specific situations. (See MCL 205.28(1)(f).) Therefore, Treasury is unable to provide information or confirmation to clients of third party administrators regarding assessments that have been paid on that third party administrator's "paid claims." Although Treasury will be unable to provide this type of information, employers, group health plan sponsors, and others using third party administrators should check with their third party administrators, who should be able to provide confirmation that the HICA assessment was properly paid with respect to claims paid on behalf of that entity.

Carriers of Medicare supplemental insurance will be subject to the HICA if they meet the definition of "carrier" in the statute and they do not fall under any of the statute's specific exemptions. (See MCL 550.1732(a).) There is no specific statutory exemption for carriers of Medicare supplemental insurance. These carriers, and claims paid pursuant to their coverage, are included in the assessment.

If the HICA collects revenue in an amount greater than \$400,000,000.00 adjusted annually by the medical inflation rate, each carrier and third party administrator that paid the assessment will receive a proportional credit to use against their assessment in the immediately succeeding year. Treasury will send a notice of credit to each HICA payer eligible to receive the credit, by July 1 of the following assessment year. Each HICA payer receiving a proportional credit should apply the credit to the next succeeding assessment periods.

HICA is repealed effective January 1, 2014.